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October Term, 1997

AT&T Corp., *et al.*,
Petitioners,
v.
Iowa Utilities Board, *et al.*,
Respondents.

AT&T Corp., *et al.*,
Petitiioners,
v.
California, *et al.*,
Respondents.

And Related Cases

On Writs of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF OF RESPONDENTS/CROSS-PETITIONERS THE MID-SIZED LOCAL EXCHANGE CARRIERS

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QUESTIONS PRESENTED

1. Did the court of appeals correctly decide that the Federal Communications Commission ("FCC") exceeded its statutory authority under the Communications Act of 1934, as amended by the Telecommunications Act of 1996 ("1996 Act"), when issuing orders and rules purporting to implement the provisions in the 1996 Act governing competition in local telephone markets?

2. Did the court of appeals correctly decide to vacate an FCC rule that, as petitioners themselves acknowledge, would allow new entrants to obtain from incumbent local telephone carriers an already combined platform of network elements at cost-based prices, when the Act allows entrants to obtain only *unbundled* network elements at cost-based prices?

3. Did the court of appeals correctly decide to vacate the FCC's rule implementing 47 U.S.C. § 252(i) as improperly subverting the system of private negotiation established by Congress?

4. Did the court of appeals err in upholding the following: (a) the FCC's ruling that entrants into the local telephone markets—without using any of their own facilities—may rely solely on the purchase of network elements, at cost-based prices, to provide local service; and (b) the FCC's expansion of the statutory definition of network elements to include Operations Support Systems, directory assistance, operator services, and vertical services?

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INTRODUCTION

This brief is filed on behalf of eight telecommunications companies that are based in virtually every part of the country, and on behalf of a trade association of telecommunications companies. Each of the companies is an incumbent local exchange carrier ("LEC"), as that term is defined in 47 U.S.C. §§ 153(26) and 251(h)(1), as added by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) ("1996 Act" or "Act").[1] The eight companies actively participated as petitioners and intervenors in the briefing and argument before the United States Court of Appeals for the Eighth Circuit and were collectively referred to as the "Mid-Sized LECs."[2] In contrast to the "large LECs," *i.e.*, the Bell Operating Companies ("BOCs") and GTE Service Corporation ("GTE"), each of the Mid-Sized LECs individually controls less than two percent of the nation's telephone access lines. The Independent Telephone & Telecommunications Alliance is a non-profit trade association representing 15 mid-sized LECs providing local exchange and exchange access telephone service in 41 states.

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[1] The relevant portions of the 1996 Act amended the Communications Act of 1934, 47 U.S.C. § 151 *et seq.* ("Communications Act"). Relevant statutes are in the appendix to the BOC's merits brief. *See also* appendix to the petition in No. 97-826 ("Pet. App."). The Mid-Sized LECs' Rule 29.6 statement is in their opposition to the petition.

[2] The "Mid-Sized LECs," and their principal places of business, are as follows: Aliant Communications Co. (Lincoln, Nebraska); ALLTEL Telephone Services Corp. (Little Rock, Arkansas); Cincinnati Bell Telephone Co. (Cincinnati, Ohio); The Concord Telephone Co. (Concord, North Carolina); North State Telephone Co. (High Point, North Carolina); Rock Hill Telephone Co. (Rock Hill, South Carolina); Roseville Telephone Co. (Roseville, California); and The Southern New England Telephone Co. ("SNET") (New Haven, Connecticut). The Mid-Sized LECs filed briefs and presented oral argument in the Eighth Circuit's review of the FCC's First Report and Order in *Iowa Utilities Bd. v. FCC*, No. 96-3321, but did not participate in the court's separate review of the FCC's Second Report and Order in *California v. FCC*, No. 96-3519. Accordingly, the Mid-Sized LECs do not address the decision in *California*.

The Mid-Sized LECs have endeavored in this brief not to repeat the arguments set forth in the merits briefs filed today by the BOCs, GTE, and the United States Telephone Association/Rural Telephone Coalition. The Mid-Sized LECs fully support those parties' arguments and incorporate them by reference in this brief. Nonetheless, as some of the approximately one thousand smaller local telephone companies throughout the United States, the Mid-Sized LECs have a unique perspective on the issues raised in this case. In their Statement, the Mid-Sized LECs describe the background, language, and structure of the 1996 Act, which underscores the central role that Congress envisioned state utility commissions would play in implementing the Act's broad goals. The Statement further discusses the progress that state regulators have made in opening local telephone markets to competition in the manner prescribed by Congress. Finally, the Mid-Sized LECs focus their Argument on the Eighth Circuit's decision regarding provisions of the Act that have been virtually ignored by petitioners, and that further demonstrate that Congress did not intend the FCC to issue detailed, uniform, national rules that bind state commissions and stifle state regulators' ability to implement the 1996 Act in the manner Congress intended.

STATEMENT

In enacting the Telecommunications Act of 1996, Congress followed the lead of numerous states that had already taken steps to open their local telephone markets to competition. Congress did so by preempting any remaining state laws that prohibited competition with incumbent local exchange carriers and by requiring incumbent LECs to, among other things, permit new entrants to interconnect with their networks and gain unbundled access to discrete elements of those networks. In passing the Act, however, the 104th Congress expressly sought to promote local competition through a deregulatory and decentralized approach. That approach relied first upon voluntary negotiations between potential competitors and, second, upon state commission-run arbitrations of issues that the parties

were unable to resolve among themselves. Congress thus sought to take advantage of the knowledge and experience of state regulators, who had long regulated local exchange service—what the Government in the past has described as the "paradigmatic intrastate market"[3]—and who best understood the regulatory history, needs and conditions of the diverse local markets and the over 1,000 incumbent LECs providing local exchange service throughout the United States. While Congress granted the FCC statutory authority to regulate with respect to certain provisions of the Act, Congress expressly preserved the authority of state utility commissions to implement the broad goals of the Act through their own regulations, applied in state commission-run arbitrations when private negotiations failed. Moreover, Congress carefully limited the power of the FCC to preempt those state regulations. In this way, Congress recognized and preserved the historical authority of state commissions as the primary regulators of local telephone markets, permitting the FCC to step in and regulate only when the states failed to execute their responsibilities under the Act.

As described below, the FCC chose to ignore Congress's deregulatory and decentralized scheme. The FCC placed itself in complete control of every local telecommunications market throughout the country by issuing uniform national rules that inhibited negotiations and preempted any and all state regulatory policies that differed in any way from those rules. The Eighth Circuit properly concluded that in doing so, the FCC had far exceeded its statutory authority under the Act.

A. Regulation of Local Telephony Before the Telecommunications Act of 1996

1. State regulation of local telephone service. Since the invention of the telephone in 1876, most local tele-

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[3] In the unsuccessful Application to Vacate Stay it filed in this Court, the FCC made the following statement: "On its face, Section 251 pervasively regulates many aspects of local exchange services, the paradigmatic intrastate market." Application to Vacate Stay at 22, *FCC v. Iowa Utilities Bd.*, No. A-299 (filed Oct. 24, 1996).

phone service has been provided to business and residential customers within a defined geographic area by a single company. Currently, over 1,000 incumbent LECs of widely varying sizes provide local exchange service in countless markets throughout the country. See H.R. Rep. No. 104-204, at 49-50 (1995), *reprinted in* 1996 U.S.C.C.A.N. 10. The Mid-Sized LECs alone range in size from approximately 90,000 to two million access lines as of December 1, 1995; by comparison, the BOCs and GTE range from approximately 14 to 21 million access lines.[4] The local markets served by the incumbent LECs differ dramatically not only in terms of their geography, but also in their topography, demographics, infrastructures, and population densities. Having regulated the LECs throughout much of that more than a century-long time period, state utility commissions are uniquely attuned to the market- and company-specific particularities that materially affect the needs of consumers of local telephone service and the pricing and even physical configuration of service in the local market.

Until recently, it was generally accepted that the provision of local telephone service was a natural monopoly, *i.e.*, that a single telecommunications provider could supply telephone service at a lower cost than could two or more firms. *See* J. Gregory Sidak & Daniel F. Spulber, *Deregulatory Takings and Breach of the Regulatory Contract*, 71 N.Y.U. L. Rev. 851, 867 (1996). Consistent with this widely-held belief, local telephone service has been a regulated monopoly for most of the century, with states enacting legislation protecting incumbent LECs against competitive entry. The right to operate as the exclusive provider of telephone services within a particular market, however, was not without countervailing costs and obligations to the provider. The states, through their utility commissions, have strictly regulated the price and

[4] United States Telephone Ass'n, *Phone Facts* 8-9 (1996), *reprinted in* Appendix to Brief of Mid-Sized Local Exchange Carriers at A-213, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Nov. 18, 1996).

service offerings of intrastate telephone service and imposed "universal service" obligations on LECs, requiring carriers to serve their entire service areas—the densely populated as well as the remote—and all of their citizens, business and residential customers alike. As a result, state regulators have built numerous cross-subsidies into the rate structures of each local exchange market. Any pricing methodology now adopted to unravel those subsidies, therefore, must be designed and implemented in a manner best adapted to the particular local market in order both to achieve vigorous competition *and* maintain universal service to all residents of each local market.

Although most LECs have historically functioned as monopolies within their own geographic markets, virtually every state is served by more than one LEC. For example, 150 incumbent LECs serve Iowa alone.[8] Consequently, state commissions have decades of experience regulating not just the retail prices that LECs charge their customers, but *interconnection* between and among the various LECs under their jurisdictions as well. Without interconnection, a family served by one LEC in a particular town would be unable to place a *local* telephone call to another family served by a different LEC in a neighboring town. Most state commissions have thus developed considerable familiarity with the technical and economic issues that arise when more than one telephone company provides service (although not overlapping service) in the same local telephone market.

As far back as 1934, when Congress passed the Communications Act and created the FCC, Congress recognized and respected the important historical role that state utility commissions had long played as the regulators of intrastate telephone service. Section 2(b) of the Communications Act, which the 1996 Act did not amend, provides that "nothing in this [Act] shall be construed to

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[8] United States Telephone Ass'n, *Phone Facts* 7 (1996), *reprinted in* Appendix to Brief of Mid-Sized Local Exchange Carriers at A-212, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Nov. 18, 1996).

apply or to give the [FCC] jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier . . . ." 47 U.S.C. § 152(b). Although the plain language of this section hardly needed any clarification, the Court, in *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355 (1986) [hereinafter *Louisiana PSC*], confirmed that section 2(b) is a "sweeping" limitation on the FCC's statutory authority that "fences off from FCC reach or regulation intrastate matters—indeed, including matters 'in connection with' intrastate service." *Id.* at 370.

In short, the Communications Act created a dual regulatory regime for telecommunications services, with the FCC given statutory authority to regulate only the interstate aspects of such services. Congress chose to allow the states to retain their historical authority as the sole regulators of intrastate telecommunications services.

2. The development of competition in local telephone markets. Competition in the telecommunications industry began developing in the 1970s in the markets for telephone equipment, information services and long-distance services. S. Rep. No. 104-23, at 2 (1995). Accelerated by the 1984 breakup of AT&T, competition for long-distance services developed and grew. In view of the increasing success of competition in the long-distance market, and with cable companies in particular recognizing that they were well positioned to offer local telephone service, many states began to investigate the prospects of bringing competition to the local exchange market. For example, as early as 1994 the Connecticut legislature had acted to open all telecommunications markets in Connecticut to competition. *See* Conn. Gen. Stat. § 16-247a *et seq.* Further, that state's principal local exchange carrier had already signed a comprehensive agreement with governmental agencies and with numerous competitors (including petitioners AT&T and MCI) governing many aspects of interconnection, network unbundling and physical collocation, leading the state utility commission in 1995 to

comment in approving the agreement that it constituted "irrefutable evidence of the ability to achieve reasonable agreement on issues of common concern to the industry and the public." *In re The Southern New England Telephone Company*, Docket No. 94-10-02, 1995 WL 807764 (Conn. D.P.U.C. Sept. 22, 1995).[6]

Connecticut was hardly alone. Beginning in earnest in 1993 and 1994, numerous states acted to bring competition to their local telephone markets. For example, the Alabama state utility commission entered a local competition order after a full-scale hearing on September 20, 1995.[7] The North Carolina commission entered a similar pro-competition order in 1996, establishing rules governing interconnection, requests for unbundled elements, resale of local service, number portability and certification of competitive local exchange carriers.[8] The North Carolina commission has certified 11 competitors, with 11 more applications pending. New York, Illinois and California also took steps in that time period to open their local markets to competition. S. Rep. No. 104-23, at 5 (1995).[9]

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[6] *See also In re The Southern New England Telephone Company's Cost of Providing Service*, Docket No. 94-10-01, 1995 WL 509180 (Conn. D.P.U.C. June 15, 1995) (order of Connecticut commission certifying 15 companies to provide local exchange service).

[7] *Order Adopting a Telecommunications Price Regulation and Local Competition Plan*, 164 P.U.R. 4th 324, 1995 WL 627739 (Ala. P.S.C. Sept. 20, 1995).

[8] *Order Setting Out Regulatory Structure for Competing Local Providers and Promulgating Rules*, Dkt. P-100, Sub 133, 1996 WL 593672 (N.C. U.C. Sept. 18, 1996) (generic docket implementing House Bill 161 on local competition).

[9] *E.g., Interim Order*, 167 P.U.R. 4th 349, 1995 WL 767890 (Cal. P.U.C. Dec. 20, 1995) (order of California Commission certifying 31 carriers to offer facilities-based local exchange services); *Order re: Competition for Local Exchange Service*, 163 P.U.R. 4th 155, 1995 WL 467996 (Cal. P.U.C. July 24, 1995); *Interim Opinion*, 1996 WL 223624 (Cal. P.U.C. Apr. 10, 1996) (California Commission holding that state regulations concerning number portability are consistent with the Act).

B. The Telecommunications Act of 1996

1. Congress ends the legal telephone monopoly. With knowledge of the states' progress toward deregulation of local exchange markets, Congress passed section 101 of the Telecommunications Act of 1996, which amended the Communications Act by adding new sections 251 through 261, codified at 47 U.S.C. §§ 251-261. Pet. App. 98a-130a. Congress intended that this new part of the Communications Act would provide the citizens of all states the benefits of competition in all sectors of the telecommunications industry, including local exchange service.

At the heart of the local telephone service provisions added by the Act is section 253, by which Congress brought an end to state and local laws giving local telephone providers legal monopoly status. Section 253 thus prohibits all state and local legislation or regulation that prohibits, or has the effect of prohibiting, any entity from providing any interstate or intrastate telecommunications service. 47 U.S.C. § 253(a). Congress recognized, however, that new entrants could not duplicate an incumbent's entire local network infrastructure overnight. It therefore imposed upon incumbents the duty to allow new entrants to interconnect their own facilities with the incumbent's network factilities and to obtain unbundled access to elements, or pieces, of the incumbent's network. 47 U.S.C. § 251(c)(2), (3). As a result, new entrants do not have to duplicate the entire local network infrastructure of loops and switches in order to compete for an incumbent LEC's customers. Instead, new entrants with at least some facilities of their own can interconnect those facilities with the incumbent LEC's local network and can purchase selected pieces of the incumbent's network facilities, without having to construct a complete local exchange network. As an alternative, Congress provided that new entrants without any facilities could purchase an incumbent LEC's finished telephone service and resell it under its own name. 47 U.S.C. § 251(c)(4).

Congress understood, of course, that it could not require incumbent LECs to open their private networks to new entrants without complying with the Fifth Amendment. The Act therefore provides that incumbent LECs can charge rates for interconnection and unbundled access that are "just, reasonable, and nondiscriminatory" and can charge wholesale rates to new entrants seeking only to purchase and then resell an incumbent's finished telephone service. 47 U.S.C. § 251(c)(2)-(4).

2. Congress's deregulatory approach to competition. Congress described the twin goals of the 1996 Act as establishing a "pro-competitive, *de-regulatory* national policy." Joint Explanatory Statement of the Committee of Conference, H.R. Conf. Rep. No. 104-458, at 1, 113 (1996) (emphasis added) (also issued as S. Conf. Rep. No. 104-230 (1996)), *reprinted in part in* 1996 U.S.C.C.A.N. 124 [hereinafter, *Joint Explanatory Statement*]. Congress envisioned that the Act would "reduc[e] regulation of the telecommunications industry . . . [to] spur the development of new technologies and increase investment in these industries." S. Rep. No. 104-23, at 9 (1995); *see id.* at 10 ("By reducing regulation and barriers to competition, the bill will help ensure the future growth of these industries"). The Act thus reflected Congress's "belief that more competition, rather than more regulation, will benefit all consumers." H.R. Rep. No. 104-204, at 50 (1995).

Consistent with its deregulatory approach, Congress consciously and explicitly designed a regime for increasing competition in the local telephone market that provides new entrants with access to the incumbent carrier's existing network and then relies principally upon private, freely negotiated agreements between the entrants and incumbents to determine the precise terms and scope of that access. Thus, the Act requires incumbent LECs and their competitors to negotiate in good faith the terms and conditions of local interconnection and access. 47 U.S.C. §§ 251(c)(1), 252(a)(1). Underscoring its preference for a deregulatory, negotiation-based approach to com-

petition, Congress even provided that the parties could enter into agreements "without regard to the [interconnection and access] standards set forth in subsections (b) and (c) of section 251." *Id.* § 252(a)(1).

In the event voluntary negotiations did not resolve all issues between the parties, Congress provided two alternatives. First, it gave the parties the option of asking a state commission "to participate in the negotiation and to mediate any differences arising in the course of the negotiation." *Id.* § 252(a)(2). Second, it provided that either party to a negotiation may "petition a State commission to arbitrate any open issues." *Id.* § 252(b)(1). Even then, Congress emphasized voluntary negotiation by prohibiting a petition to arbitrate until 135 days after the start of negotiations. *Id.*

3. Congress's decentralization of regulatory authority and preservation of state regulation. Consistent with its adoption of a deregulatory policy for bringing competition to local markets, the 104th Congress also chose a decentralized approach to government regulation of the newly opened local markets. Rather than vesting the FCC with primary responsibility to oversee implementation of the 1996 Act in countless local markets, involving over a thousand local carriers, Congress explicitly placed such authority in the state commissions that were most familiar with those markets and carriers.

Thus, Congress expressly preserved the authority of state commissions to issue regulations implementing the broad standards of the Act (47 U.S.C. § 261(b)) and forbade the FCC from preempting state commission regulations and policies governing the interconnection and access obligations of LECs that were consistent with the broad standards of the Act. *Id.* § 251(d)(3). Congress also vested state commissions with sole responsibility for determining and establishing rates for interconnection and access, including the price of unbundled network elements and wholesale rates for resold services. *Id.* § 252(c)(2), (d). In addition, as previously noted, Congress chose state com-

missions to mediate and, if necessary, arbitrate disputes between LECs and new entrants, and left to state commissions the sole responsibility to approve or reject interconnection and access agreements finalized and submitted by the parties. *Id.* § 252(a)(2), (b), (c). Congress further provided that any party aggrieved by the determination of a state commission with respect to an interconnection agreement could seek review of that determination, not with the FCC, but in federal district court. *Id.* § 252 (e)(6). Congress also foresaw that certain obligations of the Act would place small and mid-sized incumbent LECs at a grave disadvantage when suddenly faced with competition from large, sometimes global entities. It thus gave state commissions the sole authority and broad discretion to modify or suspend Congress's interconnection and access provisions where, among other things, the provisions are "unduly economically burdensome." *Id.* § 251(f)(2).

In short, in numerous provisions of the Act, Congress preserved state commission authority to continue regulating local telephone markets and expressly provided for state commissions, not the FCC, to make critical decisions concerning rates, modifications and waivers, and other local competition matters under the Act. As discussed at greater length under the first Argument heading, Congress's choice to leave regulatory authority principally in the hands of state regulators was deliberate, as reflected not only in the statutory text, but also in the Act's legislative history.

C. The FCC's Rulemaking

The FCC was unwilling to abide by Congress's twin decisions to encourage competition by relying principally on private negotiation backed by state commission mediation and arbitration, and to leave critical regulatory authority over pricing, waivers and other aspects of opening the local markets to competition to the state utility commissions. The FCC even ignored Congress's choice of federal district court review for state commission decisions,

expressly inviting aggrieved parties instead to seek review of those decisions before the FCC.

While some may consider statutory interpretation to be a creative endeavor, it is beyond dispute that the interpretive process should begin with the text of the statute itself. *See Staples v. United States,* 511 U.S. 600, 114 S. Ct. 1793, 1797 (1994); *Northern States Power Co. v. United States,* 73 F.3d 764, 766 (8th Cir. 1996). Yet the FCC rejected this fundamental rule of statutory interpretation in construing the 1996 Act. Instead, the FCC brought a set of presumptions to its interpretation of the Act that have no basis in the language or structure of the Act. Those presumptions led the FCC to imagine that Congress had granted it plenary authority to regulate all aspects of local telecommunications markets, to the virtual exclusion of state regulation. The FCC's predisposition to interpret the Act in this way was first evident in the agency's Notice of Proposed Rulemaking ("NPRM"), published in the Federal Register on April 25, 1996. J.A. 303. There, the FCC announced that the Act created a "new regulatory paradigm" for telecommunications and that Congress intended the FCC, through its rulemaking, to breathe life into that paradigm. J.A. 305. The FCC also announced that the only possible way to bring competition to local telecommunications markets would be through the promulgation of uniform, national rules, since such rules would supposedly produce certain efficiencies that might not be obtained if the state commissions were left to make their own decisions and promulgate their own rules for their home markets. J.A. 313-15.

The FCC's presumptions, while visible in the NPRM, were elevated to a fundamental premise of every aspect of the agency's First Report and Order [hereinafter FRO]. J.A. 403. Paying lip service to Congress's deliberate and bargained-for choice of a deregulatory and decentralized approach to opening local telecommunications markets to competition, the FCC, on August 8, 1996, issued a 700-

page, single-spaced decision that sets forth in minute and mind-numbing detail the agency's view of how it would have brought competition to local markets if it had written the Act. Exploiting what it saw as an opportunity to break from the legal shackles that for decades have barred it from regulating intrastate telecommunications, the FCC issued an order and rules that were revolutionary in scope. Explicit in its mammoth order is the FCC's view that Congress had chosen the FCC to be the new chief regulator and overseer of every local market in the country and that the FCC alone had the knowledge and expertise to determine the future of the numerous local markets and approximately 1,000 incumbent LECs throughout the United States. From the FCC's perspective, uniform national rules—which only it could promulgate—were absolutely essential to efficient implementation of the Act, and without such rules, chaos would reign in local markets and incumbent LECs would purposefully inhibit or delay the efforts of new entrants. FRO ¶¶ 50, 56, 102, 104-20, 179, 625 (J.A. 429, 432, 455-65, 495-96, 721).

In the First Report and Order, two additional critical presumptions of the FCC emerged: (1) Congress's preference for a private, voluntary negotiation-based approach to establishing interconnection and access agreements would never work; and (2) state commissions could not be trusted to fulfill the responsibilities that Congress had expressly entrusted to them under the Act. It would not be unfair to say that the First Report and Order as a whole reflects, at best, a patronizing attitude toward state commissions, and, at worse, utter contempt towards states. This view persists in the Government's briefs as well. For example, in briefs submitted in the Eighth Circuit, the FCC made no apologies for its conclusion that absent its own particular national rules, state commissions "likely would tilt [the terms of competitive entry] in the incumbent monopolists' favor." Mem. of FCC & USA in Opp. to Mot. for Stay at 3, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Sept. 20, 1996).

Indeed, one month before the release of the First Report and Order, the then-Chairman of the FCC candidly admitted that the agency was seeking to consign state regulation of local exchange markets to the "trash can of history." *See* Interview with Reed Hundt, *in* Telecommunications Report, Supp. at 10 (July 9, 1996).

Chairman Hundt was right about the FCC's purpose in issuing the First Report and Order. The following are just several of many examples of the FCC's disdain for state regulation of local telephone markets and for the choices made by Congress in enacting the Act:

- Whereas Congress chose voluntary negotiations as the preferred method of achieving interconnection agreements between incumbent LECs and new entrants (47 U.S.C. § 252(a)(1)), and required incumbent LECs to bargain with new entrants in good faith (*id.* § 251(c)(1)), the FCC concluded that incumbents had no "economic incentive . . . to provide potential competitors with opportunities to interconnect with and make use of the incumbent LEC's network and services." FRO ¶ 55 (J.A. 432). The agency therefore decided that it had no choice but to impose "proxy" prices that, by its own admission, were "presumptive ceilings" that would restrict the scope of voluntary negotiations. *Id.* ¶ 768 (J.A. 790-91).

- Whereas Congress, in 47 U.S.C. § 251(d)(3), expressly constrained the FCC's authority to preempt state interconnection and access regulations and policies, the FCC pronounced *ex cathedra* in a single paragraph of its 700-page First Report and Order that "state regulations that are inconsistent with our rules *may* 'substantially prevent implementation of the requirements of this section and the purposes of [Part II of Title II]'." FRO ¶ 102 (J.A. 456) (emphasis added) (quoting 47 U.S.C. § 251(d)(3)).

- Whereas Congress, in 47 U.S.C. § 251(f)(2), expressly granted state commissions the authority to suspend or modify any of the requirements of 47

U.S.C. § 251(b), (c) for small and mid-sized LECs if a state commission found the requirement to be "unduly economically burdensome" to the LEC, the FCC narrowly restricted the suspension and modification authority of state commissions to situations where the requirement "would be likely to cause undue economic burden *beyond the economic burden that is typically associated with efficient competitive entry.*" 47 C.F.R. § 51.405(d) (emphasis added).

- Whereas Congress expressly provided in 47 U.S.C. § 252(c)(2), (d) that state commissions would determine and establish the rates for interconnection and unbundled access to network elements, the FCC established a uniform, national pricing methodology and announced that state commissions were required to adhere to that methodology. FRO ¶ 111 (J.A. 461-62).
- Whereas Congress expressly provided in 47 U.S.C. § 252(e)(6) that a party aggrieved by a determination of a state commission may appeal to the appropriate federal district court, the FCC announced that an aggrieved party "may elect to either bring an action for federal district court review *or* a section 208 complaint to the Commission against a common carrier." FRO ¶ 128 (J.A. 468) (emphasis added).[10]

Together, these regulatory pronouncements of the FCC reflect an agency that simply cannot conceive of a world in which Congress has legislated to open local telecommunications markets to competition but has not given the FCC the central role. In the face of provision after provision of the Act in which Congress gave state commissions, not the FCC, primary regulatory and oversight authority, the FCC audaciously sought to transform a six-month time limitation on issuance of FCC regulations in

[10] Section 208 merely gives the FCC jurisdiction to hear complaints "of anything done or omitted to be done by any common carrier." 47 U.S.C. § 208. As argued below, that statute does not authorize FCC review of the regulatory actions taken by state commissions.

section 251(d)(1) into a sweeping and unprecedented grant to the FCC of plenary authority to establish binding regulations regarding *all* aspects of telecommunications services in *all* local markets. With an arrogance that apparently knows no bounds, the FCC announced that its interpretation "is the *only* reasonable way to reconcile the various provisions of sections 251 and 252, and the statute as a whole." FRO ¶ 84 (J.A. 448) (emphasis added).

The FCC was correct that the Act did create a "new regulatory paradigm" in the sense that Congress had decided for the first time to put an end to local telephone providers' legal monopoly and to open all local telephone markets to competition. The Commission fundamentally erred, however, in concluding that Congress had placed the FCC at the center of that paradigm. In fact, Congress had opted to rely principally upon private negotiations, backed up by state commission mediations and arbitrations, as the means of implementing the broad goals of the Act.

D. The Court of Appeals' Decision

On October 15, 1996, the Eighth Circuit, in response to motions of several parties, granted a stay of the FCC's pricing and "pick-and-choose" rules pending final review on the merits.[11] J.A. 224. The FCC and other petitioners applied to this Court twice to vacate the stay, but the Court declined to interfere with the Eighth Circuit's stay. 117 S. Ct. 379 (1996) (Thomas, J., in chambers); 117 S. Ct. 429 (1996). Accordingly, the FCC's pricing rules have not been in effect for nearly two years. After extensive briefing and several hours of oral argument, the court of appeals issued its full decision on the merits on July 18, 1997, and amended that decision on rehearing on October 14, 1997. No party has applied to this Court for a stay of the court of appeals' decision.

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[11] By order dated September 27, 1996, the Eighth Circuit entered an interim stay of the First Report and Order pending a decision on the motions for stay, so that the rules would not go into effect while the court considered the motions.

In stark contrast to the FCC, whose interpretation of the Act proceeded from the belief that competition could never occur in the absence of its own uniform national rules and that state commissions could not be trusted to execute their responsibilities under the Act, the Eighth Circuit focused its analysis on the plain language of the Act. Moreover, unlike the FCC, the Eighth Circuit engaged in that analysis unfettered by any desire to be at the center of the new local telephone market playing field. It also emphasized at the outset that its "review [did] not encompass any determination regarding the wisdom or prudence of the policies Congress set forth in the Act, those considerations being the Constitutionally-assigned prerogatives of the Legislative Branch of our national government." Pet. App. 8a.

Relying upon the plain language of 47 U.S.C. § 252 (c)(2), (d), the court of appeals held that the Act "undeniably authorize[s] the state commissions to determine the prices an incumbent LEC may charge for fulfilling its duties under the Act." Pet. App. 11a. The court also held that the FCC's blanket preemption of all state rules and regulations that were in any way inconsistent with its own regulations was invalid in light of section 251(d)(3). As the court observed, "The FCC's blanket statement that state rules must be consistent with the Commission's regulations promulgated pursuant to section 251 is not supportable in light of subsection 251(d)(3). With subsection 251(d)(3), Congress intended to preserve the states' traditional authority to regulate local telephone markets and meant to shield state access and interconnection orders from FCC preemption so long as the state rules are consistent with the requirements of section 251 and do not substantially prevent the implementation of section 251 or the purposes of [the Act]." Pet. App. 39a-40a.

The court further held that the FCC had exceeded its statutory authority in promulgating regulations restricting the authority of state commissions under 47 U.S.C. § 251 (f)(2) to modify or suspend certain requirements of the Act for small and mid-sized LECs. Pet. App. 27a-30a.

And the court disagreed with the FCC's claim of authority under 47 U.S.C. § 208 to review interconnection agreements approved by state commissions, holding instead that Congress vested regulatory authority over interconnection agreements solely in the state commissions, subject to a right of appeal to the appropriate federal district court. Pet. App. 30a-34a. In short, the Eighth Circuit rejected the FCC's exaggerated perception of the agency's authority under the Act.

In addition, the Eighth Circuit considered the validity of certain FCC rules concerning the unbundled access and resale provisions of the Act. The FCC took the position in the First Report and Order that a new entrant without any facilities of its own could provide finished telephone service by purchasing from an incumbent *all* of the network elements required to provide such service. FRO ¶¶ 328-41 (J.A. 571-76). The incumbents had argued that the FCC's position eviscerated the distinction between 1) the resale provisions of the Act, pursuant to which a new entrant could purchase an incumbent's finished telephone service at wholesale rates; and 2) the unbundled access provisions, pursuant to which a new entrant could purchase network elements at cost-based rates. Specifically, the incumbents argued that by permitting new entrants to purchase all of the network elements necessary to provide finished telephone service at cost-based rates, the FCC had rendered the resale provisions of the Act a nullity, since no rational new entrant would pay higher wholesale rates for a service that it could purchase at cost.

The Eighth Circuit agreed with the incumbent LECs that any valid interpretation of the Act needed to recognize and maintain the purposeful distinction made by Congress between resale and purchase of unbundled network elements. Pet. App. 71a. Nevertheless, the court upheld the FCC's ruling in the First Report and Order that a new entrant may purchase all of the network elements needed to provide finished telephone service. The court concluded that its vacatur of 47 C.F.R. § 51.315(b)-(f)—which contrary to 47 U.S.C. § 251(c)(3) required incumbents

(rather than requesting carriers) to recombine network elements that are purchased by the requesting carriers on an unbundled basis—would be sufficient to maintain Congress's distinction. Pet. App. 56a-57a, 70a-71a.

E. Impact of the FCC's Rules and the Court of Appeals' Decision on Competition

Consistent with their view that the states cannot be trusted and that private, voluntary negotiations between incumbents and new entrants, backed by state commission arbitrations, cannot work, petitioners predictably claim that the Eighth Circuit's decisions, including its earlier stay of the pricing rules, are somehow responsible for any delay in the achievement of full competition in the local markets. *See, e.g.*, AT&T Pet. 12. Nothing could be further from the truth. Indeed, the Assistant Attorney General in charge of the Justice Department's Antitrust Division has recently testified that competition in the local exchange markets is proceeding forward as fast as one could expect in such a complex matter.[12] The FCC has also elsewhere praised the states for largely adopting on a voluntary basis the FCC's pricing methodology.[13] If, as it contends, most states have *voluntarily* followed the FCC's pricing methodology, the FCC can hardly claim that the Eighth Circuit's decision that the FCC may not *require* states to adopt its preferred methodology has frustrated the pro-competition goals of the Act. To the extent that there has been any undue delay in accomplishing what Congress recognized would be the difficult, complex and time-consuming task of opening all telecommunications

[12] Joel I. Klein, *Bringing Competition to Local Telephony: The Department of Justice's Perspective*, Statement before the Senate Judiciary Committee, Subcommittee on Antitrust, Business Rights, and Competition (Mar. 4, 1998) ("The fact that the market is being opened—albeit more quickly in some places than in others—seems clear from the fact that entrepreneurs are seizing the opportunity to enter a $100 billion market heretofore closed to competition").

[13] *See, e.g.*, Reed Hundt, Chairman, FCC, remarks to the Chamber of Commerce, Washington, D.C. (May 29, 1997) (as prepared for delivery) ("[V]irtually every state in the Union has adopted our [pricing] policies").

markets to full competition,[14] it is attributable in large measure to the FCC's own misguided attempts to displace the pro-competition efforts of various states and to new entrants' singular focus on trying to pick off only lucrative business customers instead of investing in the facilities or services necessary to provide quality local service to all local customers—residential and commercial alike.[15]

Thus, in the months after Congress passed the Act, many state commissions had already moved to adopt rules and policies designed to foster interconnection and access in the manner envisioned by Congress, and many parties were in the process of negotiating agreements to provide interconnection and access. The FCC itself recognized in the NPRM that as of 1996, 19 states had already taken action to open local markets to competition, including seven states in which competing firms had already begun to offer switched service. J.A. 306. *See supra* at notes 6-9 and accompanying text. Moreover, in a contested proceeding after passage of the Act, the Connecticut DPUC concluded that its actions in setting standards for interconnection, unbundled access and resale competition—including its methodology for determining just and reasonable rates—were consistent with the Act.[16] As the Eighth Circuit found, however, the FCC's adoption of its rules, and its attempt to dictate every conceivable contract term and preempt every state rule on pricing and other aspects of interconnection, was leading to the break-

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[14] *See* H.R. Rep. No. 104-204, at 72 (1995); *see also* Statement of FCC Chairman Reed Hundt on S. 1822, the Communications Act of 1994, United States Senate (Feb. 23, 1994).

[15] *See, e.g.*, J. Keller, *AT&T's New Chief Plans Bold Agenda*, Wall Street J., Dec. 3, 1997, at A3 (reporting that AT&T's new CEO is laying groundwork for possible mega-merger); M. Mills, *WorldCom Would Shift MCI's Focus*, Washington Post, Oct. 3, 1997, at A1 (quoting WorldCom's Vice Chairman; "Our strategy is not in the consumer business"); *WorldCom Makes Unsolicited $29 Billion Stock Bid For MCI*, Communication Daily, Oct. 2, 1997 (reporting on WorldCom's $29 billion bid for MCI).

[16] *See In re The Southern New England Telephone Co.*, Docket No. 95-11-08, 1996 WL 497056 (Conn. D.P.U.C. July 17, 1996).

down of negotiations and, absent a stay, would have "derail[ed] current efforts to negotiate and arbitrate agreements under the Act." J.A. 238 (ruling on motions for stay); *see also* Pet. App. 10a n.9.

The Eighth Circuit issued its stay of the pricing and "pick and choose" provisions to permit the negotiations and arbitrations envisioned by the Congress to proceed. And proceed they did. The fact is that nearly 200 interconnection agreements had been signed by February 1997, within four months of the Eighth Circuit's stay opinion. By November 1997, just 20 months after passage of the Act, over 280 companies had voluntarily signed well in excess of 1,700 interconnection agreements to provide local service of some kind in over 450 cities through the country.[17] It should hardly be surprising to anyone that with thousands of interconnection agreements and numerous arbitrations, there should be (as petitioners claim) between 70 and 100 review proceedings in the federal district courts.

Not only have companies negotiated and signed interconnection agreements, but they have also begun to offer local telephone service under the watchful oversight of state commissions, precisely in the manner envisioned by Congress. For example, in Connecticut—one of the first states targeted by petitioners such as AT&T, MCI and others for local competition[18]—the state utility commis-

[17] United States Telephone Ass'n, *Competition Report* (Nov. 3, 1997) (the "*USTA Competition Report*") (*see* Appendix to the Mid-Sized LECs' Brief in Opposition to Petitions for Certiorari at A-1); New Paradigm Resources Group, Inc. and Connecticut Research Group, Inc., 1997 Annual Report on Local Telecommunications Competition (8th ed. 1997).

[18] *See* K. Donnelly, *MCI Celebrates the Anniversary of Connecticut Local Telecommunications*, Business Times—New Haven, Connecticut, May 1997, at 1; S. Higgins, *AT&T Goes Local With Service Today*, New Haven Register, Mar. 1, 1997, at A1 (reporting that "AT&T chose Connecticut for its first major thrust" into local markets); B. Keveney, *TCI Service to Expand Next Month*, Hartford Courant, Dec. 20, 1995, at A3 (reporting that TCI chose Hartford for one of its first forays into local telephone competition).

sion has certified over 36 companies to provide local exchange service and over 200 companies to offer intrastate toll services, and it has ruled that beginning in January 1999 every residential and small business customer of respondent SNET, the incumbent local carrier, will be required to select by ballot which carrier from among SNET and the many certified new entrants it wishes to use for local telephone service. *In re DPUC Investigation of The Southern New England Telephone Company*, Docket No. 94-10-05 (Conn. D.P.U.C. June 25, 1997), *as revised by* Final Decision (Conn. D.P.U.C. Dec. 22, 1997) (not available on Westlaw); *see also DPUC Administration of the Local Exchange Co. Election Process*, Docket No. 97-08-12 (Conn. D.P.U.C., docket opened Aug. 27, 1997) (developing technical standards for balloting in meetings that include representatives of new entrants). Nine of the 36 certified local exchange carriers are currently offering local telephone service in Connecticut, including petitioners AT&T and MCI. Similar competition is occurring in other states' markets. All of this progress toward competition in local markets has occurred without the FCC dictating pricing methodologies to the state commissions and competing carriers and without the FCC preempting every state policy or rule on intervention and access that differs from the FCC's own rules.[10] That progress will continue if the Eighth Circuit's decision is affirmed.

SUMMARY OF ARGUMENT

The Mid-Sized LECs do not question the wisdom of introducing competition to the local exchange market. The question is on whose terms will that competition take

[10] For example, respondent Cincinnati Bell Telephone Co. has voluntarily negotiated and entered into, and has arbitrated, numerous interconnection agreements in Ohio, Kentucky and Indiana. MCI and Time Warner are already providing facilities-based local telephone service in Cincinnati. The Nebraska Public Service Commission has certified 13 companies as Local Competition carriers and approved 19 interconnection agreements. *See USTA Competition Report.*

place. Contrary to the position of the FCC, the Mid-Sized LECs, like the Eighth Circuit, believe that it is Congress's terms that should govern.

In constructing its pro-competition, deregulatory framework for ensuring that citizens of all states share in the benefits of competition in local telecommunications markets, Congress expressly eschewed a single set of detailed national rules, recognizing that all local markets and all LECs are not the same—that solutions that work in New York City or in Los Angeles might be disastrous in Des Moines or Fargo, and that requirements that might merely annoy a large national LEC might threaten the very existence of a small or mid-sized LEC. Congress, therefore, sought to take advantage of the local knowledge and experience of state utility commissions in regulating their home markets by giving them, among other powers: (1) the exclusive authority to establish prices where the parties themselves have failed to agree; (2) the sole responsibility to modify or suspend portions of the Act for small and mid-sized LECs; and (3) the explicit right to continue to design and apply their own locally sensitive regulatory policies to ensure fulfillment of the Act's goals. *See* 47 U.S.C. §§ 251(d)(3), (f)(2), 252(c)(2), (d), 261(b).

The 104th Congress would not recognize the detailed, centralized edifice designed by the FCC as the pro-competitive, deregulatory program that Congress passed in February 1996. As the Eighth Circuit correctly recognized, the underlying premise and rationale of the FCC's approach to its jurisdiction over pricing and non-price rules relating to local competition is fundamentally at odds with the language, structure and legislative history of the Act. Under the FCC's vision, the system of private negotiations desired by Congress, backed up by state-run mediation or arbitration, is the wrong way to encourage competition in local markets. Thus, instead of reducing regulatory costs and burdens through private negotiation and preserving traditional state control over countless local

markets and providers of local telephone service, the FCC rules impose a new layer of agency regulation and bureaucratic micro-management. The FCC's rules radically shift local telecommunications regulation from the states to Washington, D.C.; they disable small and mid-sized incumbent LECs from remaining vigorous and innovative competitors in the markets they know best and currently serve; and they inhibit the facilities-based competition that permits companies to distinguish themselves by price, service and technology, the essential ingredients of true competition. In short, as the Eighth Circuit recognized, the FCC's rules are neither pro-competitive nor deregulatory in purpose or effect.

ARGUMENT

I. CONGRESS NARROWLY CIRCUMSCRIBED THE FCC'S REGULATORY AUTHORITY OVER LOCAL TELEPHONE SERVICE.

Petitioners' briefs have two points in common. First, their jurisdictional arguments proceed from a shared premise: because Congress passed legislation to open local telephone markets to competition in states that had not already undertaken that effort on their own, Congress must also have intended that the FCC would have plenary authority to oversee implementation of the 1996 Act. Second, petitioners apparently hope that by merely labeling a host of discrete statutory issues as "jurisdictional," they can obtain review and reversal of the Eighth Circuit's decision on those issues without actually addressing each part of the court's decision in their briefs. These issues include: (1) whether the FCC has authority under 47 U.S.C. § 251(d)(3) to preempt *en masse* all regulatory policies of state commissions enforcing the interconnection and access obligations of section 251; (2) whether the FCC has any power under 47 U.S.C. § 251(f)(2) to constrict the authority given by Congress solely to state commissions to modify or suspend the requirements of section 251(b) or (c) for small and mid-sized LECs; and

(3) whether, under 47 U.S.C. § 208, the FCC may review the decisions made by state commissions when arbitrating, approving or rejecting interconnection agreements under section 252, even though 47 U.S.C. § 252 (e)(6) provides solely for judicial (not FCC) review of state commission determinations.

Contrary to the claim of petitioners, in opening local markets to competition, Congress did not grant the FCC plenary authority to regulate those markets to the virtual exclusion of state commissions who had historically exercised that important responsibility. Instead, as the Mid-Sized LECs show in Part I.A. below, Congress purposely chose an approach that preserved the regulatory authority of state commissions. This is seen not only in the Act's delegation of pricing authority to state commissions, a subject thoroughly explored in the briefs of the BOCs and GTE filed today, but also in the other sections of the Act listed above. These provisions show that Congress made numerous conscious choices about the division of responsibility between federal and state regulators during the drafting and debate of the legislation. As the language and legislative history of each section reveals, Congress consistently chose to amend pending legislation to leave regulatory authority in the hands of state regulators—and not just on pricing issues. Viewed collectively, these additional sections of the Act put the lie to petitioners' claim —which they use specifically to support their pricing jurisdiction arguments—that the guiding principle of the 104th Congress was to replace state regulation of local telephone markets with centralized FCC control from Washington.

Petitioners are also wrong in their apparent belief that if the Eighth Circuit's pricing jurisdiction ruling is reversed, the Court must necessarily also reverse the Eighth Circuit's separate rulings vacating the FCC's construction and application of sections 251(d)(3), 251(f)(2), and 252(e)(6), cited above. In Part I.B., the Mid-Sized LECs address the specific text of each of these critical sec-

tions that petitioners largely ignore in their briefs.[20] Petitioners should not be able to obtain relief in this Court on these matters of great importance without separately addressing the merits of each of these sections.[21] Each of these issues was extensively briefed and argued before the Eighth Circuit and was the subject of a separately reasoned ruling by that court under separate headings in its opinion. Pet. App. 27a-34a, 36a-40a. The Eighth Circuit did not link the different parts of its decision together, so that each would fall if any one of them fell. That court

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[20] Petitioners mention the Eighth Circuit's decision on these sections only in passing, in footnotes or in parenthetical references in text, devoting virtually all of their argument on FCC "jurisdiction" to the question of whether the Eighth Circuit erred in vacating the FCC's rules concerning pricing. For example, the only parties who discuss the Eighth Circuit's ruling on the scope of section 251(d)(3) are the FCC (Br. 22-23) and respondent GST Telecom, Inc. in support of petitioners (Br. 9-10). Neither the FCC nor GST Telecom, however, devote more than two paragraphs of their briefs to the section. Also, the FCC addresses only in a string cite, without discussion, the Eighth Circuit's ruling on the FCC's rule governing waivers under section 251(f)(2), and the Eighth Circuit's ruling on the FCC's purported authority under section 208 to review state commission determinations under section 252. FCC Br. 26 n.9. Other petitioners give the subject little attention in their arguments. MCI Br. 38 (one paragraph on section 208); AT&T Br. 21 (reference to section 251(f)(2) in string cite); AT&T Br. 31 (one paragraph on section 208).

[21] Petitioners' improper stratagem of sweeping every Eighth Circuit ruling they do not like into their argument on pricing jurisdiction is starkly exposed in AT&T's brief. AT&T takes issue with parts of the Eighth Circuit's decision that vacated FCC rules on wholly non-jurisdictional grounds, even though those parts of the decision are not subsumed in any of the questions presented by AT&T or any other petitioner. AT&T Br. 32-34. AT&T is simply wrong that the Eighth Circuit's decision on these issues was affected by its jurisdictional holding. For example, the Eighth Circuit vacated an FCC rule requiring incumbent LECs, upon the request of a competitor, to provide interconnection and access to the competitor that is superior in quality to what the incumbent provides itself. The court's decision was based on "the plain terms of the Act," Pet. App. 51a, and cannot in any way be described as a "jurisdictional" ruling, as AT&T claims.

understood, as petitioners fail to recognize, that it could not decide the validity of all of the FCC's orders and rules solely on the basis of a discussion of the FCC's power to issue rules generally or pricing rules in particular. The court correctly grounded each of its rulings in the text and legislative history of the particular provision of the Act in question, and not just in the FCC's jurisdictional authority generally as petitioners claim in their briefs. The court's rulings should therefore be affirmed.

A. The Act Preserves State Commission Authority to Regulate the Local Telephone Market.

1. In section after section of the local competition provisions of the 1996 Act, Congress, as it did in the 1934 Act, expressly preserved the historical role of state utility commissions as the regulators of local telephone markets and the numerous companies that provide local service in those markets. Thus, in recognition of the leading role that many states had played in developing regulations and policies that fostered local competition, Congress explicitly barred the FCC in section 251(d)(3) from "preclud[ing] the enforcement of any regulation, order, or policy of a State commission that—(A) establishes access and interconnection obligations of local exchange carriers; (B) is consistent with the requirements of this section; and (C) does not *substantially prevent* implementation of the requirements of this section and the purposes of this part [§§ 251-261]." 47 U.S.C. § 251(d)(3) (emphasis added).

In section 261(b), Congress emphasized more generally that state commissions have a critical responsibility to implement the federal statute. Section 261 provides that nothing in the Act "shall be construed to prohibit any State commission from enforcing regulations prescribed prior to February 8, 1996, or from prescribing regulations after such date of enactment, *in fulfilling the requirements of this part*, if such regulations are not inconsistent with the provisions of this part [§§ 251-261]." *Id.* § 261(b) (emphasis added). In addition, section 252(e)(3) provides that "subject to section 253 [of this title], nothing in

this section shall prohibit a State commission from establishing or enforcing other requirements of state law in its review of an [interconnection] agreement, including requiring compliance with intrastate telecommunications service quality standards or requirements." 47 U.S.C. § 252(e)(3). Sections 253(b) and (c) further confirm the state's continued authority to "preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers" and to "manage the public rights-of-way." 47 U.S.C. § 253(b), (c). And, significantly, section 601(c)(1) of the 1996 Act (not codified in Title 47) provides that "[t]his Act . . . shall not be construed to modify, impair, or supersede Federal, State, or local law unless expressly so provided . . . ."

Congress also recognized that certain obligations of the Act could place small and mid-sized incumbent LECs at a grave disadvantage when suddenly faced with competition from large, global entities and that state utility commissions, with their knowledge of local markets and local companies, were best positioned to determine whether smaller companies in those local markets needed relief from the Act's requirements. Accordingly, in section 251(f)(2), Congress gave state commissions the sole authority and broad discretion to modify or suspend Congress's interconnection and access provisions where, among other things, they were "unduly economically burdensome," 47 U.S.C. § 251(f)(2), so that companies with far fewer resources than "large global or nationwide entit[ies]" could effectively adjust to the new competitive environment. S. Rep. No. 104-23, at 22 (1995). In crafting the waiver provision, the Senate Committee stated:

> The Committee intends that *the . . . State* shall, consistent with the protection of consumers and allowing for competition, use this authority to provide a level playing field, particularly when a company or carrier to which this subsection applies faces competition from a telecommunications carrier that is a large glo-

> bal or nationwide entity that has financial or technological resources that are significantly greater than the resources of the company or carrier.

Id. (emphasis added).

The text of provisions such as sections 251(d)(3), 261(b) and 251(f) thus affirm the primacy of state commissions as not only the regulators of the local telecommunications markets, but also the regulators of first resort in implementing the broad local competition standards in section 251. Congress's message could not have been clearer: except where expressly provided, the Act does not preempt state commission regulations designed to open local markets to competition. To the extent that Congress granted the FCC any regulatory authority in section 251, Congress explicitly barred the FCC from exercising that authority to preclude enforcement of a state commission's own regulations and policies, unless the FCC finds that the regulations and policies: (1) are inconsistent with the broad standards in section 251 (not the FCC's own regulations); or (2) substantially prevent implementation of the requirements of section 251 and the purposes of the local telephone competition provisions of the 1996 Act.

Section 252 further confirms the Act's orientation toward state regulation of competition in the local exchange market. As noted above, Congress provided that state commissions would mediate and, if necessary and requested by a party, arbitrate open issues between parties negotiating interconnection agreements. 47 U.S.C. § 252(a)(2), (b). In addition to giving state commissions these integral roles in ensuring that private parties reach agreement on interconnection matters, through mediation and arbitration, Congress left to state commissions the sole authority to approve or reject interconnection agreements once they are finalized and submitted by the parties. 47 U.S.C. § 252(e). Congress further provided that any party aggrieved by a determination of a state commission under section 252 "may bring an action in an appropriate Federal district court to determine whether the agreement . . .

meets the requirements of Section 251 and this section." 47 U.S.C. § 252(e)(6).

In those instances when the parties are unable to agree on issues generally, and request arbitration, Congress directed state commissions to ensure that resolution of those issues meets the requirements of section 251, including any of the FCC's validly promulgated and enforceable regulations under section 251. Section 252, however, included requirements wholly apart from those in section 251, and which Congress directed state commissions alone to enforce when conducting arbitrations. In particular, Congress directed state commissions to "establish any rates for interconnection, [resold] services, or network elements according to subsection (d) [of section 252]." 47 U.S.C. § 252(c)(2). In subsection (d), Congress set forth the specific factors that a state commission must use when it makes its rate "[d]eterminations." 47 U.S.C. § 252(d)(1)-(3). Significantly, the provisions of section 252 that directly authorize the state commissions to establish prices in arbitrations are devoid of any reference to FCC regulations.

2. It was no accident that Congress largely preserved traditional state authority over the local exchange market and that it gave state commissions exclusive authority over pricing issues. Rather, it was a purposeful choice reflected in numerous sections of the Act and in its legislative history. Like most legislation, "the Act was the product of many successful compromises among a variety of competing views and interests, and reflects the customary give and take of the legislative process." [22] Perhaps nowhere in the Act, however, are the outcomes of those legislative compromises more clear than in the text of many of the above provisions, as passed by Congress and signed into law by the President. In one provision after another, Congress removed language referring to or giving the FCC

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[22] Brief of Amici Curiae Congressman Bliley, *et al.*, at 3, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Dec. 23, 1996); *see also* Brief of Amici Curiae Congressman Dingell, *et al.*, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Nov. 15, 1996).

regulatory authority over issues that fundamentally affect the local exchange market.

For example, Congress rejected earlier versions of section 251(f)(2) that had provided for *dual* FCC/state commission authority over decisions to modify or suspend interconnection and access obligations for small and mid-sized LECs, concluding instead that those decisions required a thorough knowledge of the small and mid-sized LECs and the local markets and should thus be handled exclusively by state commissions. *See* S. Rep. No. 104-23, at 22, 93 (1995) (§ 251(i)); H.R. Rep. No. 104-204, at 74, 144 (1995) (§ 252(e)). Thus, on the day that the Senate passed the Act, Senator Daschle (the minority leader) remarked: "The bill before us also recognizes the important role that must be played by Public Utilities Commissions (PUC's) in *rural States.* PUC's are the best entities to judge whether a given market within their State can support competition. *That's not a judgment we should make from Washington.*" 142 Cong. Rec. S709 (daily ed. Feb. 1, 1996) (emphasis added).

Similarly, the House amended H.R. 1555 on the day it passed that bill to add the precursor to section 251(d)(3), which "[p]reserve[s] state access regulations." The House version was identical in every respect to the final text of section 251(d)(3) as later amended in Conference and enacted into law, except that the House originally sought to uphold the enforceability of state commission regulations, orders and policies regarding interconnection and access obligations only if they would "not substantially prevent *the* [*FCC*] from fulfilling the requirements of this section and the purposes of this part." 141 Cong. Rec. H8444, cols. 2-3 (daily ed. Aug. 4, 1995) (inserting new subparagraph (B) in House Commerce Committee's version of section 242(b)(4), reprinted in 141 Cong. Rec. H8427, col. 1) (emphasis added). However, in response to concerns expressed by state commissions,[23] the Confer-

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[23] The Chair of the Wisconsin Public Service Commission expressed her concern in a letter to Representative Watts that the House bill reported out of committee wrongfully expanded the

ence deleted reference to the FCC in the above-quoted phrase, leaving section 251(d)(3) as preserving state regulations, orders and policies that do "not substantially prevent implementation of the requirements of this section and the purposes of this part." In short, section 251(d)(3) confirms the states' independent role in executing Congress's plan to introduce competition to the local markets of all states. That role is further confirmed by section 261(b)'s general preservation of state commission authority to promulgate regulations that fulfill the requirements of the local telephone provisions of the 1996 Act, independent of any regulations that the FCC might also promulgate (pursuant to the limited authority Congress gave the FCC).

The legislative history of the Act also confirms what the language and structure of sections 251 and 252 show—that Congress made a conscious choice to reserve exclusive control over pricing issues to state commissions. Earlier versions of the 1996 Act had given the FCC control over pricing, but those provisions were modified in Conference to place pricing standards under the control of state commissions under a new section 252. *See Joint Explanatory Statement* at 13; *see generally id.* at 117-26. In the bill that was enacted into law, Congress made numerous clear distinctions between "the requirements" of section 251 and the separate "requirements of section 252," including the pricing standards set forth in section 252(d). *See, e.g.*, 47 U.S.C. §§ 251(c)(2)(D), (c)(3), 252(e)(2)(B). Although Congress sometimes referred to FCC rules when also referring to the requirements of section 251, it never referred to such rules when separately

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FCC's authority and that the "manager's amendment" on the House floor, which added the precursor to section 251(d)(3) discussed above in text, "does not give us everything we had asked for, [but] it certainly does a better job of balancing federal and state jurisdiction." The state commission Chair further wrote that "[to] the extent that your efforts would give the states a stronger chance to gain some ground *on the jurisdictional issues in conference committee*, I would tend to support your efforts." 141 Cong. Rec. H8453 (daily ed. Aug. 4, 1995) (emphasis added).

referring to the pricing standards of section 252. *See, e.g., id.* § 252(c)(1), (c)(2), (e)(2)(B), (f)(1), (f)(2).[24]

3. Congress did not leave the FCC without any role to play under the 1996 Act. The requirements of section 251 include several specific references to FCC regulations under that section.[25] At the same time, however, section 251(d)(3) expressly preserves the ability of the state commissions themselves to implement the interconnection and access requirements of section 251, so long as their policies are in keeping with the text of section 251 and the overall purposes of the local competition part of the 1996 Act. On those specific subjects where Congress has authorized the FCC to implement section 251, the FCC may preclude enforcement of a state commission's policies, but only if those state policies do not satisfy the broad guidelines of the Act. Nowhere does section 251(d)(3) reference FCC regulations. Moreover, Congress preserved state commissions' exclusive authority to implement the requirements of section 252, including the arbitration and approval of interconnection agreements and the setting of prices in arbitration. Congress provided that if, but only if, a state commission fails to execute its responsibilities under section 252 with respect to a particular matter, the FCC "shall issue an order preempting the State commission's jurisdiction of that proceeding or matter

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[24] For example, in 47 U.S.C. § 252(e)(2)(B), Congress provided that a state commission may reject an interconnection agreement adopted by arbitration only if the state commission "finds that the agreement does not meet the requirements of Section 251, including the regulations prescribed by the [FCC] pursuant to Section 251, or the standards set forth in subsection (d) of this section." While the FCC plainly has some regulatory authority under section 251, the breadth of that authority is limited, as described more fully in the briefs filed by the BOCs and GTE.

[25] *E.g.*, 47 U.S.C. § 251(b)(2) (number portability); *id.* § 251(c)(4)(B) (prohibitions on resale); *id.* § 251(d)(2) (network elements); *id.* § 251(e) (numbering administration); *id.* § 251(g) (exchange access); *id.* § 251(h) (treatment of comparable carriers and incumbents).

. . . and shall assume the responsibility of the State commission under this section [252] with respect to the proceeding or matter and act for the State commission." 47 U.S.C. § 252(e)(5).

Put another way, Congress gave the FCC the role of backup regulator of the local exchange market. In those states where regulators are willing and able to take affirmative steps to open their local markets to competition consistent with the broad guidelines established by the Act, Congress permitted those regulators to continue to exercise their historical control without interference from the FCC. However, in states where regulators have abdicated that responsibility and are unwilling either to enforce the congressional mandates of section 251 or to undertake their regulatory responsibilities in section 252 to arbitrate disputes or review interconnection agreements, the FCC may regulate in lieu of the state commission as if it were the state commission. In this way, Congress preserved the historical role of the state commissions as regulators of intrastate telecommunications service, while ensuring that all citizens enjoy the benefits of local competition by permitting the FCC to fill any void left by states that had not acted to open their local markets to competition.[26]

The plain language and legislative history of numerous sections of the Act thus undermine the central premise of petitioners' jurisdictional arguments, including their arguments on pricing—that Congress intended to bring about competition in the local exchange through detailed FCC rules on every conceivable subject that would bind all state commissions throughout the country. To the contrary, viewed as a whole, the Act establishes Congress's clear objective to preserve state commission regulatory

[26] An exception to this scheme is found in 47 U.S.C. § 251(e)(1), which grants "exclusive jurisdiction" to the FCC "over those portions of the North American Numbering Plan that pertain to the United States." That reference to the FCC's "exclusive jurisdiction" is the only such reference in section 251.

authority over local telephone markets and to deny the FCC the plenary regulatory authority over those markets that it seeks.

B. The Eighth Circuit's Rulings on the Scope of FCC Authority Under Sections 251(d)(3), 251(f)(2) and 252(e)(6) Are Consistent With the Plain Terms and Legislative History of the Act.

As discussed above, in addition to giving state commissions exclusive authority to establish the rates for interconnection and access, Congress also gave state commissions: (1) the explicit right in section 251(d)(3) to apply their own regulatory policies to implement the broad competition goals of the Act; (2) the sole authority in section 251(f)(2) to waive or modify portions of the Act for mid-sized and small LECs; and (3) the exclusive regulatory authority to approve or reject interconnection agreements, subject only to review in federal district courts under section 252(e)(6). The court of appeals' rulings on each of these sections is independently supported by the text and legislative history of each provision. Contrary to petitioners' suggestions, therefore, the Eighth Circuit's decision on each of these sections must be affirmed regardless of the Court's disposition of petitioners' arguments on the scope of the FCC's jurisdiction over pricing.

1. Section 251(d)(3) Limits Whatever Regulatory Authority the FCC May Validly Exercise to Implement the Requirements of Section 251.

The FCC argues that 47 U.S.C. § 251(d)(1) expressly grants it the statutory authority to implement every provision of the local competition portion of the Act. FCC Br. 19; *see also* AT&T Br. 23; MCI Br. 27. As the BOCs and GTE demonstrate in their briefs, Congress's direction to the FCC to establish regulations within six months cannot possibly be transformed into a revolutionary grant of plenary authority to the FCC over every aspect of intrastate telecommunications governed by section 251.[27] However-

[27] By its terms, section 251(d)(1) addresses "the requirements of this section," 47 U.S.C. § 251(d)(1), and therefore does not

ever, regardless of the subject matters that the FCC may permissibly regulate under section 251, and regardless of the statutory source of whatever regulatory authority the FCC may have, the FCC may not ignore the language of section 251(d)(3), which operates as an express limitation upon *any* FCC authority exercised to implement the requirements of section 251. Nevertheless, in its First Report and Order the FCC did just that, by issuing binding, national rules and requiring all state commissions uniformly to adhere to the FCC's rules to the exclusion of the state commission's own rules and policies that may differ from the FCC's. FRO ¶¶ 53-62, 101-03, 179 (J.A. 431-36, 455-56, 495-96). The Eighth Circuit correctly rejected the FCC's attempt to nullify Congress's clear command in section 251(d)(3) to preserve state regulation of interconnection and access. Pet. App. 36a-40a.

The FCC seeks to dismiss section 251(d)(3) as nothing more than a provision to "ensure that state commission orders consistent with federal law are not invalidated on the theory that the Commission's rules preempt a regulatory field." FCC Br. 22. That argument ignores the text of the Act. Congress made absolutely clear in section 261(b) that the Act, which necessarily includes any FCC regulatory authority thereunder, was not intended to have field preemptive effect.[28] Congress did not need to repeat

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address rulemaking by the FCC to implement the requirements of other sections, such as section 252 (including the pricing standards of section 252(d)). Consequently, section 251(d)(3), like section 251(d)(1), is properly read only to address non-pricing regulations to fulfill the requirements of section 251. However, if petitioners were correct in their erroneous argument that the FCC has authority to issue pricing rules because the requirements of section 251 supposedly incorporate by reference the pricing standards of section 252, then the anti-preemption provision of section 251(d)(3) would necessarily be equally applicable to the FCC's pricing rules.

[28] As previously noted, section 261(b) provides, "Nothing in this part [*i.e.*, sections 251-261] shall be construed to prohibit any State commission from enforcing regulations prescribed prior to February 8, 1996, *or from prescribing regulations after such date of enactment, in fulfilling the requirements of this part,* if such regulations

this point in section 251(d)(3), as the FCC's argument necessarily suggests. Instead, Congress went even further in section 251(d)(3) by limiting the FCC's power to preempt *specific* state regulations, orders or policies. It bears emphasizing that in section 251(d)(3), entitled "Preservation of state access regulations," Congress explicitly barred the FCC, when exercising whatever limited regulatory authority it possesses to implement section 251, from "preclud[ing] the enforcement of any regulation, order, or policy of a State commission that—(A) establishes access and interconnection obligations of local exchange carriers; (B) is consistent with the requirements of this section; and (C) does not *substantially prevent* implementation of the requirements of this section and the purposes of this part [*i.e.*, sections 251-261]." 47 U.S.C. § 251 (d)(3) (emphasis added). Thus, section 251(d)(3) is far more specific, and far more restrictive of FCC authority, than an anti-field preemption provision.

The FCC also claims that because section 251(d)(1) —in the FCC's view—authorizes the FCC to issue regulations to implement the provisions of section 251, the enforcement of any state regulation that is inconsistent with an FCC regulation would by definition "substantially prevent" implementation of the Act. FRO ¶ 103 (J.A. 456). Yet that assertion can succeed only if Congress intended the FCC to be the sole implementor of section 251 or if there were only one reasonable way to implement the broad goals of the Act. For several reasons, neither premise can be sustained.

First, as noted above, section 261(b)—which the FCC does not even cite, let alone discuss, in its brief—provides that state commissions may issue regulations to fulfill the requirements of the Act. In light of this section, any argument that the FCC is the sole entity that Congress authorized to implement the broadly worded goals of the Act is completely without merit. Just as important, sec-

are not inconsistent with the provisions of this part." 47 U.S.C. § 261(b) (emphasis added).

tions 261(b) and 251(d)(3) are consistent in permitting state commissions to fulfill the requirements of section 251 (and, for section 261(b), also to fulfill the requirements of section 252) *without regard to FCC regulations.* It does no good for the FCC to point to the language in 47 U.S.C. § 252(c)(1) directing state commissions to ensure that the resolution of open issues in arbitration "meet[s] the requirements of Section 251, including the regulations prescribed by the [FCC] pursuant to Section 251." Under the highly specific and sweeping terms of section 251(d)(3), FCC regulations that are otherwise proper under section 251 are not enforceable to override a state commission's own regulations and policies.[29]

Any other reading of section 252(c)(1) would write section 251(d)(3) out of the Act, which is what the FCC apparently would like to do. However, as discussed at page 31, *supra,* Congress consciously inserted section 251(d)(3) into the Act to address the concerns of state regulators. Congress did not accept the House version of section 251(d)(3) that went into the Conference Committee, which would have limited state regulation to policies that would not "substantially prevent *the FCC from fulfilling* the requirements of this section and the purposes of this part." *See* pages 31-32, *supra.* By removing "the FCC" from the final text of the section, Congress made clear its position that more than one way existed to implement section 251 and that a state regulation could differ from an FCC regulation, yet still be consistent with section 251 and not "substantially prevent" implementation of the goals of the local competition provisions of the Act. *See INS v. Cardoza-Fonseca,* 480 U.S. 421, 442-43 (1987) ("Few principles of statutory construction are more com-

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[29] As discussed *supra* at page 34 n.26, Congress did grant "exclusive jurisdiction" to the FCC "over those portions of the North American Numbering Plan that pertain to the United States." 47 U.S.C. § 251(e)(1). A state commission would therefore be bound by FCC regulations under that lone provision conferring "exclusive jurisdiction" on the FCC.

pelling than the proposition that Congress does not intend *sub silentio* to enact statutory language that it has earlier discarded in favor of other language") (internal quotations omitted).[30] In short, the FCC's argument on the meaning of section 251(d)(3) is nothing more than an effort to reverse a legislative defeat.

Second, if the FCC were correct that it has plenary power to regulate under section 251 and that the enforcement of any state regulation inconsistent with an FCC regulation would, by definition, "substantially prevent" implementation of section 251, then section 251(d)(3) would once again be a meaningless provision. Under current preemption law, if the FCC did have the plenary regulatory authority it erroneously claims, state rules that were directly inconsistent with the FCC's own rules or that stood "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *i.e.*, rules that "substantially prevented" implementation of the FCC's regulations, would be preempted without the need for section 251(d)(3) to say so. *See Fidelity Federal Savings & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 153 (1982). Congress obviously included section 251(d)(3), not as a meaningless gesture, but as an express limitation on whatever regulatory authority the FCC was given under section 251.

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[30] The FCC's construction of the statutory scheme ignores not only the legislative history of the section, but also the established principle of statutory construction that a specific statutory provision prevails over a more general provision. *See Bigger v. American Commercial Lines, Inc.*, 862 F.2d 1341, 1344 (8th Cir. 1988) (*citing MacEvoy Co. v. United States*, 322 U.S. 102, 107 (1944)); *accord Fourco Glass Co. v. Transmirra Prods. Corp.*, 353 U.S. 222, 228-29 (1957). It also ignores this Court's repeated admonition that "we start with the assumption that the historic police powers of the States [are] not to be superseded by [a] Federal Act unless that was the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947); *see Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983) ("the regulation of utilities is one of the most important of the functions traditionally associated with the police powers of the States").

The FCC also argues that there is no valid distinction between a state regulation that is inconsistent with the Act and a regulation that is inconsistent with the FCC's own application of the standards of the Act. FCC Br. 23 n.7. This argument, however, ignores the text of the interconnection and access standards of section 251, which are sufficiently general to sustain differing implementations by state commissions. The FCC and other petitioners concede as much by their reliance on the *Chevron* doctrine of deference in support of the merits of the FCC's rules, which they would not need if the statutory standards were susceptible of only a single interpretation. *See Chevron U.S.A. Inc. v. Natural Resources Defense Council,* 467 U.S. 837 (1984). Thus, as the Eighth Circuit held, a state regulation can be consistent with section 251 if it represents a reasonable approach to implementing that section's requirements, even if the state's method of implementation differs from the FCC's preferred approach. Pet. App. 37a-38a. Section 251(d)(3), therefore, represents an explicit congressional rejection of the usual rule that when a federal and state regulation are in conflict, the federal regulation always prevails.

In the First Report and Order, the FCC sought to avoid the clear implications of sections 251(d)(3) and 261(b) by attempting to discover its preemption authority in section 261(c). FRO ¶ 98 (J.A. 454). The FCC's effort to locate preemption authority in that section, however, is unavailing. Section 261(c) authorizes states to impose additional legal requirements intended to open local telephone markets to competition, so long as those requirements are consistent with this part of the Act (sections 251-261) and any regulations validly promulgated by the FCC under this part. 47 U.S.C. § 261(c). As the Eighth Circuit found, sections 261(b) and 251(d)(3)—unlike section 261(c), which addresses state laws wholly apart from the 1996 Act—deal specifically with state commission regulations that fulfill the requirements of the 1996 Act, not with *additional* state legal requirements. Pet. App. 39a. The FCC cannot minimize the import of Congress's omis-

sion in the anti-preemption provision of section 251(d)(3), and in the preservation of state commission authority in section 261(b), of any requirement that state commission regulations comport with FCC rules. *See Russello v. United States*, 464 U.S. 16, 23 (1983).

Finally, the FCC's reliance upon section 261(c) ignores the settled principle that a specific statutory provision prevails over a more general provision. Section 251(d)(3) is expressly and specifically applicable to every state "regulation, order, or policy" that "establishes access and interconnection obligations of local exchange carriers."[31] By contrast, section 261 lacks this specificity. In addition, section 261(b) expressly addresses the authority of state commissions to prescribe regulations that fulfill the requirements of the 1996 Act. Once again, section 261(c) lacks such specificity. Accordingly, where state regulation of interconnection and access obligations is concerned, section 251(d)(3) must control.

Congress's considered decision to allocate regulatory authority in this manner, and to place express limitations on the FCC's preemption power, also serves to distinguish the cases that the FCC relies upon to support its position —*City of New York v. FCC*, 486 U.S. 57 (1986), and *Fidelity Federal Savings & Loan Ass'n v. de la Cuesta*, 458 U.S. 141 (1982). In neither of those cases did Congress expressly limit the preemptive authority of the federal agency, as it so clearly did here. To the contrary, *de la Cuesta* held that the statutory language authorizing the Federal Home Loan Bank Board to regulate federal savings and loans "suggest[ed] that Congress expressly contemplated, and approved, the Board's promulgation of regulations superseding state law." 458 U.S. at 162. Similarly, *City of New York v. FCC* upheld FCC regulations that established technical standards governing the quality

[31] This reference to the "access and interconnection obligations of local exchange carriers," 47 U.S.C. § 251(d)(3)(A), is a broad, shorthand reference to the numerous obligations of LECs set forth in subsections (b) and (c) of section 251.

of cable television signals and that prohibited local authorities from imposing more stringent technical standards. In so doing, the Court noted, "[i]t is also quite significant that nothing in the Cable Act or its legislative history indicates that Congress explicitly disapproved of the Commission's preemption of local technical standards." 486 U.S. at 67. In sum, in both *de la Cuesta* and *City of New York*, the Court recognized that Congress could have limited the preemption authority of the respective regulatory agencies if it had wanted to, though in each case it did not. In the 1996 Act, however, Congress explicitly did limit the FCC's preemption authority. Congress's choice must be respected.

2. *The FCC Never Determined That Any State Regulation, Order or Policy Was Inconsistent With Section 251 or "Substantially Prevented" Implementation of the Requirement of Section 251 or the Purposes of the Act.*

For an additional reason, the Eighth Circuit correctly rejected the FCC's position that its uniform, national interconnection and access rules are binding on the states: the FCC never actually determined that any particular state regulation, order or policy was, in fact, contrary to the requirements of section 251 or would "substantially prevent" implementation of the requirements of section 251 or the purposes of the local competition provisions of the 1996 Act. To the contrary, the FCC simply pronounced in the First Report and Order that "state regulations that are inconsistent with our rules *may* 'substantially prevent implementation of the requirements of this section and the purposes of [Part II of Title II]'." FRO ¶ 102 (J.A. 456) (emphasis added) (quoting 47 U.S.C. § 251(d)(3)); *see also id.* ¶¶ 177-80 (J.A. 494-96) (new entrants need not "comply with a multiplicity of state variations" in interconnection requirements). The FCC's use of the word "may" in its order is telling and not surprising, since a "substantial prevention" finding would have been impossible given the FCC's failure to examine—or even in the

NPRM to request comments on—whether any particular state's regulations implementing section 251 had actually hindered competition in that state. The FCC simply assumed (as it has here as well), without any basis in the record, that state regulations that differed in any way from its own regulations might have that effect.[32] However, if section 251(d)(3) has any meaning at all, it is that the FCC must make specific findings and conclusions about the real impact of particular state commission regulations, orders and policies on the pro-competitive goals of the Act before issuing or enforcing preemptive regulations.[33]

Yet, the FCC did the one thing that Congress explicitly said it could not do: preempt all state regulations that differed from its own uniform, national rules without first determining whether the state regulations were consistent with section 251 or whether they substantially prevented implementation of that section or the purposes of the Act. Because it failed to take these predicate steps to a preemption order, the Eighth Circuit properly held that the "FCC's blanket statement that state rules must be consistent with the Commission's regulations promulgated

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[32] Significantly, some state commissions, such as Connecticut's Department of Public Utility Control, have expressly concluded in contested proceedings *after* passage of the 1996 Act that their rules and policies for interconnection, unbundled access to network elements and resale competition—even where different from the FCC's rules—are consistent with the 1996 Act and its goals. See page 20 n.16, *supra*.

[33] Because the FCC did not develop *any* record on the effect of state interconnection and access rules on competition, the FCC's defense of its preemption ruling in this proceeding is necessarily limited to establishing that *all* state commission regulations, orders and policies that differ in any way from the FCC's rules must be preempted on their face. In other words, to uphold the FCC's actions and reverse the Eighth Circuit, this Court would have to find that there is no possible set of circumstances under which a state commission's actions that varied from the FCC's rules would satisfy the requirements of section 251(d)(3). *See California Coastal Comm'n v. Granite Rock Co.*, 480 U.S. 572, 580, 588-89 (1987). There is no basis for making that finding on this record.

pursuant to section 251 is not supportable in light of section 251(d)(3)." Pet. App. 39a.

3. *The FCC Unlawfully Restricted State Commissions' Statutory Authority to Modify or Suspend Obligations for Small and Mid-Sized LECs.*

Further underscoring Congress's confidence in the states, 47 U.S.C. § 251(f)(2) gives to state commissions alone the authority to suspend or modify the requirements of section 251(b) or (c) in certain circumstances for LECs in their state that serve fewer than two percent of the nation's subscriber lines.[34] Those circumstances include when the LEC can demonstrate in a petition filed with the state commission that section 251(b) or (c) imposes "a requirement that is unduly economically burdensome."[35] In purporting to construe section 251(f)(2), the FCC issued Rule 405(d), which impermissibly narrows the circumstances under which Congress intended that a smaller LEC may obtain relief from the requirements of section 251(b) or (c). The rule does so by requiring smaller LECs to prove that a section 251 requirement "would be likely to cause undue economic burden *beyond the economic burden that is typically associated with efficient competitive entry.*" 47 C.F.R. § 51.405(d) (emphasis added) (Pet. App. 307a-308a). Rather than interpreting

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[34] Under section 251(f)(2), only LECs with fewer than two percent of the nation's subscriber lines in the aggregate qualify for this "2% waiver" provision. That definition includes all of the Mid-Sized LECs. The Mid-Sized LECs have a unique interest in the application of this provision because, unlike smaller, rural LECs that make up the vast majority of LECs in this country, many of the Mid-Sized LECs do not qualify for the automatic rural exemption of 47 U.S.C. § 251(f)(1)—a provision addressed at length in the Brief for the United States Telephone Association and Rural Telephone Coalition ("USTA Brief"), which brief the Mid-Sized LECs fully endorse.

[35] The "unduly economically burdensome" test is just one of three alternative tests in section 251(f)(2) for justifying a waiver, but the FCC conceded below that its rules neither address nor purport to limit a LEC's right to resort to the other two tests.

the statute, the FCC's rule changed the text of the statute, by adding words of limitation to the straightforward phrase used by Congress in the statute.

In other words, if "efficient competitive entry"—the FCC's phrase, not Congress's—would "typically" cause the demise of the smaller LEC with a strong historical tie to its service area, due to the entry of a multinational competitor with no long-term commitment to that area, the FCC's rule would disable the state commission from even temporarily suspending or modifying any of the requirements of section 251. Yet, that scenario is precisely what Congress intended would satisfy the "unduly economically burdensome" test for waivers under section 251 (f)(2). *See* pages 28-29, *supra.* By definition, the numerous small and mid-sized LECs are not "typical," but are each characterized by a unique history and market. The statutory phrase, and not the one made up by the FCC, governs when a state commission may tailor a requirement to the uniquely local situation to *enhance* competition by ensuring the local company's survival.

These defects in the FCC's rule are not surprising given the FCC's own conclusion that its rulemaking record did not afford the agency a sufficient basis to establish national rules governing section 251(f). In its First Report and Order, the FCC found "convincing assertions that it would be an overwhelming task at this time for the Commission to try to anticipate and establish national rules for determining when our generally-applicable rules should *not* be imposed upon carriers." FRO ¶ 1253 (emphasis in original) (J.A. 1020). That finding—which the FCC then promptly ignored by issuing Rule 405(d) as a binding, national rule—comported with Congress's intent in enacting section 251(f), which gives the FCC *no* role to play in that purely local decision. Indeed, Congress deleted any reference to FCC jurisdiction in section 251 (f)(2) and decided instead that waiver decisions requiring a thorough knowledge of small and mid-sized LECs should be handled *only* by state commissions, which are

best equipped to make such determinations on a company-by-company basis, and not from Washington. *See* page 31, *supra*. Once again, the FCC may not claim authority specifically rejected by Congress. *Cardoza-Fonseca,* 480 U.S. at 442-43.

The Eighth Circuit therefore did not need to address the merits of the FCC's rule when vacating it as beyond the FCC's statutory authority. The Eighth Circuit relied on the express statutory text and clear legislative history of section 251(f)(2), which vested regulatory authority over waivers solely in state commissions, and the court independently supported its decision by reference to section 2(b) of the Communications Act. Pet. App. 28a. For these reasons, and for the reasons set forth in USTA's brief, there are no grounds to disturb the Eighth Circuit's ruling vacating Rule 405(d), either on the basis of the text of section 251(f) itself or on broader, jurisdictional grounds.

4. *The FCC Unlawfully Ordered That Parties Aggrieved by a State Commission Determination Under Section 252 May Bypass District Court Review and Seek Review Directly From the FCC.*

In yet another usurpation of a power that Congress did not grant the FCC, the FCC ruled in the First Report and Order that any party dissatisfied with the action taken by a state commission under section 252 to approve or reject a negotiated or arbitrated interconnection agreement may seek review of that state action before the FCC. FRO ¶¶ 121-29 (J.A. 465-69). However, as with its pricing and waiver provisions, Congress nowhere granted the FCC this regulatory power. In section 252, Congress placed each state commission—not the FCC—at the center of responsibility for overseeing the efforts of private parties to enter into agreements for local interconnection, network elements, or services. If negotiating parties remain unsatisfied after a state has acted to arbitrate, approve, or reject interconnection agreements, Congress expressly em-

powered the federal district courts, not the FCC, to review state commission determinations.

Congress could not have made its intent clearer. Thus, section 252(e)(6), entitled "Review of State commission actions," states:

> In any case in which a State commission makes a determination under this section, any party aggrieved by such determination may bring an action *in an appropriate Federal district court* to determine whether the agreement or statement meets the requirements of section 251 of this title and this section.

47 U.S.C. § 252(e)(6) (emphasis added). Congress provided only one venue, "an appropriate Federal district court," for parties aggrieved by state commission determinations.

Despite this clear congressional mandate, the FCC once again sought power that Congress did not give it, and it therefore added words and requirements that Congress never enacted. Thus, while the Act states that parties aggrieved by a state commission determination have a single option, the FCC "conclude[d] that parties have several options for seeking relief." FRO ¶ 124 (J.A. 467). And while the Act states that aggrieved parties must seek review in a federal district court, the FCC "conclude[d] that a person aggrieved by a state determination under sections 251 and 252 of the Act may elect to either bring an action for federal district court review *or* a section 208 complaint to the Commission against a common carrier." *Id.* ¶ 128 (J.A. 468) (emphasis added). Moreover, the FCC made it clear that its assertion of review authority would not be limited to determining whether a common carrier has complied with a state commission determination. It would also extend to reviewing carrier actions *"even if the carrier is in compliance with an agreement approved by a state commission." Id.* ¶ 127 (J.A. 468) (emphasis added). In other words, the FCC claims plenary authority to review the terms of state-approved interconnection agreements.

The statutory mechanism for negotiating and approving interconnection agreements under section 252 excludes any direct, or even indirect, oversight role by the FCC. Congress relied on state commissions alone to mediate or arbitrate open issues during negotiations, and regardless whether the parties reach agreement solely through negotiation or through a combination of negotiation and arbitration, Congress required that the agreement be submitted to the state commission for approval or rejection. 47 U.S.C. § 252(e)(1). Congress also specified the standards to be followed by the state commission in determining whether to approve or reject agreements. *Id.* § 252(e)(1)-(4). The state commissions, therefore, have exclusive jurisdiction to determine the validity of such agreements, subject only to review by a federal district court. *Id.* § 252(e)(6).

Congress authorized the FCC to exercise authority over interconnection agreements in one limited instance—where the state commission fails to exercise its responsibilities under section 252. The sole provision authorizing FCC involvement in the process is section 252(e)(5), entitled "Commission to act if State will not act." This statute provides:

> If a State commission fails to act to carry out its responsibility under this section in any proceeding or other matter under this section, then the Commission shall issue an order preempting the State commission's jurisdiction of that proceeding or matter within 90 days after being notified (or taking notice) of such failure, and shall assume the responsibility of the State commission under this section with respect to the proceeding or matter and act for the State commission.

Id. § 252(e)(5). The title and explicit language of this provision could not be clearer: the FCC may enter this area of state concern only if the State commission does not fulfill its specific statutory responsibilties. Even then, the FCC is limited to exercising the same authority that the state commission may exercise under section 252.

These words are unambiguous and must be the starting and ending point of statutory interpretation.

Because Congress expressly excluded the FCC from any role in reviewing state commission determinations, the Court must reject the FCC's attempt to justify its power grab by concocting a new interpretation of its jurisdiction over complaints against interstate common carriers under 47 U.S.C. § 208, a provision that predates the 1996 Act. The FCC's conclusion that "[s]ection 252(e)(6) does not divest the Commission of jurisdiction, in whole or in part, over complaints that a common carrier violated section 251 or 252 of the Act," FRO ¶ 126 (J.A. 468), is premised upon the FCC's mistaken belief that its generalized section 208 complaint jurisdiction already provides the agency with power to adjudicate the new rights, responsibilities and procedures Congress detailed in the Act.

Section 208 does no such thing, for three fundamental reasons. First, the FCC has repeatedly stated that it does not have section 208 jurisdiction to hear complaints relating to *intrastate* matters. *See, e.g., Just Aaron*, 10 FCC Rcd. 11519 (1995); *ACC Long Distance Corp.*, 8 FCC Rcd. 85 (1993); *HAP Services, Inc.*, 2 FCC Rcd. 2948 (1987). As the FCC itself has acknowledged, local exchange service is the "paradigmatic intrastate market." *See* page 3 n.3, *supra*.

Second, the express language of section 208 does not support expanded FCC jurisdiction. That section gives the FCC general jurisdiction to supervise wrongs done by "common carriers." Nothing in that section purports to grant authority to review and override the decisions of a state utility commission. Complaints regarding the arbitration, approval or rejection of an interconnection agreement are all complaints about the state commission's determinations under section 252. The FCC's novel ruling on the scope of section 208 therefore collides with the plain meaning of that provision.

Third, nothing in the Act demonstrates that Congress intended to expand the FCC's complaint jurisdiction under section 208. The FCC therefore relied on an argument

that Congress, in the general savings clause in section 601(c) of the Act (uncodified in Title 47), somehow indirectly modified the express provision for federal district court review in section 252(e)(6), *and* expanded the jurisdictional reach of section 208 to intrastate matters.[36] Again, that assertion of jurisdiction rests entirely upon a contorted and improper reading of section 208 as governing state regulatory action, and an indifference toward Congress's choice that parties aggrieved by state commission actions may seek review only in federal district courts.

The Eighth Circuit overturned the FCC's ruling regarding the scope of its complaint jurisdiction under section 208. The court held that traditional rules of statutory construction require interpreting Congress's choice of federal district court review of state commission decisions as the exclusive means of review. Pet. App. 31a-32a (citing cases). The absence of any reference in section 252 to FCC review reinforced the court's conclusion in this regard. *See id.* at 33a. The court correctly noted:

> The only grant of any review or enforcement authority to the FCC is contained in subsection 252(e)(5), and this provision authorizes the FCC to act only if a state commission fails to fulfill its duties under the Act. The FCC's expansive view of its authority under section 208 is thus contradicted by the language, structure, and design of the Act.

Id. Only after rendering its conclusion based on "the language, structure, and design of the Act" did the court separately and independently hold that section 2(b) of the Communications Act *also* precludes the FCC from exer-

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[36] In the First Report and Order, the FCC stated: "Section 601(c)(1) of the 1996 Act provides that the 1996 Act 'shall not be construed to modify, impair or supersede' existing federal law—which includes the section 208 complaint process—'unless expressly so provided.' Sections 251 and 252 do not divest the Commission of its section 208 complaint authority." FRO ¶ 126 (J.A. 468). Additionally, the FCC seized on the fact that Congress in section 252(e)(6) omitted the word "exclusive" when it expressly gave jurisdiction to the federal courts to review state determinations. *Id.* ¶ 124 (J.A. 467).

cising authority under section 208 to review state commission decisions on interconnection agreements. It so held because many aspects of those agreements, such as pricing, are outside the FCC's jurisdiction. *See id.* at 33a-34a. The Act's general savings clause in section 601(c) is hardly the straightforward and unambiguous grant of intrastate authority that *Louisiana PSC* requires. *See* 476 U.S. at 377.

Following Congress's explicit choice to limit review of state commission decisions to the federal district courts is particularly important for small and mid-sized LECs. These LECs are especially vulnerable to efforts by large well-financed entrants to grind them down through multiple and duplicative regulatory proceedings. The FCC cannot ignore Congress's plainly expressed intention that parties to an agreement need only pass one regulatory hurdle—the state commission—when entering into interconnection agreements. Accordingly, the FCC should not be permitted to seize regulatory authority over interconnection agreements through the back door of section 208, when Congress itself directly denied the FCC such authority under the Act. The Eighth Circuit was therefore correct to reject the FCC's effort to rewrite section 252 by placing review of state commission determinations within the FCC's jurisdiction.

C. The Text and Structure of the Act as a Whole Undermine Petitioners' Argument that the Act Necessarily Gives the FCC Power to Issue Binding National Rules on Pricing Matters.

As this discussion has demonstrated, there is no basis for petitioners' arguments that Congress rejected the historical model of local telephone regulation and sought to concentrate regulatory authority over the local markets in the FCC. The FCC can argue all it wants that regulation by fiat from Washington is supposedly the most "efficient" way to ensure competition. Congress had other interests to balance when it passed the 1996 Act.

Rather than address all of petitioners' pricing jurisdiction arguments in this brief, the Mid-Sized LECs fully support and incorporate by reference herein the arguments of the BOCs and GTE concerning the FCC's lack of statutory authority to promulgate national pricing rules. It should come as no surprise that Congress listened to the wishes of those who sought to keep pricing authority in the local market solely in the hands of state regulators, where it had always been. Even the FCC concedes that under the Act state commissions retain exclusive regulatory authority over retail rates for local telephone service. FCC Br. 32 n.12. It is hardly a leap in logic to conclude that the 104th Congress had sufficient confidence in the knowledge and abilities of state regulators to permit them to maintain exclusive regulatory authority over the rates that incumbents charge to new entrants as well. After all, the Act expressly states that wholesale rates shall be based upon the retail rates that even the FCC concedes state commissions, and state commissions alone, may set. *See* 47 U.S.C. § 252(d)(3) ("a State commission shall determine wholesale rates on the basis of retail rates"). Furthermore, a key input to any determination of a retail rate is the price charged for interconnection and network elements. Given the state commissions' experience and know-how in analyzing the cost and profit structures of each of the over 1,000 incumbent LECs, it was logical for Congress to give the state commissions exclusive authority to determine the inputs to retail rates in addition to the retail rates themselves.[87]

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[87] Congress's enactment of a statute preserving state regulatory authority subject to newly enacted federal standards is not novel, and contrary to the claims of petitioner MCI (Br. 40), poses no constitutional problems. *See, e.g., Hodel v. Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 288-89 (1981) (upholding statute against constitutional challenge), *cited in Printz v. United States*, 117 S. Ct. 2365, 2380 (1997). If a state chooses not to continue to regulate its local telephone market in the manner prescribed in the Act, Congress provided that the FCC would then, and only then, assume the responsibilities of the state commission. 47 U.S.C. § 252(e)(5).

This Court should therefore affirm the Eighth Circuit in its decision to vacate the FCC's pricing rules and the other FCC orders and regulations discussed in Part I of this Argument. Each aspect of the court of appeals' decision, whether it involves pricing, preemption, waivers, or review of state commissions, is independently supported by the text, structure and legislative history of the specific statutory provision at issue and the local competition part of the 1996 Act generally. Furthermore, the court of appeals' well-reasoned construction of section 2(b) of the Communications Act independently supports each aspect of its decision. Though each ruling by the court of appeals on the various orders and regulations stands alone, the court's rulings also support each other and are internally consistent, as they fit with Congress's overall desire to introduce competition into the local telephone markets, not by detailed one-size-fits-all national rules promulgated by the FCC, but by voluntary negotiation and, only when necessary, by state regulation subject to federal district court review.

II. THE FCC'S UNBUNDLING RULES EVISCERATE THE RESALE PROVISIONS OF THE ACT.

There is no disagreement that the Telecommunications Act of 1996 establishes distinct modes for opening local telephone markets to competition for new entrants that lack some or all of the network facilities needed to provide local service—interconnecton with, and use of, unbundled elements of the incumbent's network, or resale. FRO ¶ 12 (J.A. 413). Nor can there be any disagreement that Congress intended the Act to promote facilities-based competition. As one member who later sat on the Conference Committee put it, "it is no exaggeration to say that the entire bill is premised on the existence of robust facilities-based competition." Hearings before House Subcomm. on Telecommunications & Finance of the House Comm. on Commerce, 104th Cong., Serial No. 104-34, at 9 (daily ed. Aug. 4, 1995); *see also* 141 Cong. Rec. H8465 (daily ed. Aug. 4, 1995) (the Act is intended to

"give[] new entrants the incentive to build their own local facilities-based networks, rather than simply repackaging and reselling the local services of the local telephone company"). To encourage facilities-based competition, however, the Act established distinct pricing standards for the two very different modes of competition. Thus, the Act allows new entrants seeking to compete through the use of their own incomplete network facilities to fill in the gaps in those facilities by purchasing, *at cost-based rates,* discrete elements from an incumbent's network. By contrast, those new entrants seeking to compete with an incumbent LEC by doing nothing more than purchasing finished retail telephone services from the incumbent and reselling the services must pay the incumbent a statutorily defined discount from the retail rate (*i.e.*, a *wholesale rate*) to buy the finished service.

There is a disagreement of the most fundamental nature, however, about the impact of the FCC's unbundled access rules upon Congress's careful distinction between resale and the purchase of unbundled network elements. The Mid-Sized LECs and other cross-petitioners contend that the FCC's rules—which permit a new entrant to obtain from a LEC at cost-based rates a fully assembled platform containing all of the network elements necessary to provide finished telephone service—render the resale provisions of the Act a nullity. For if a requesting carrier could simply purchase all of the pre-assembled network elements that an incumbent LEC uses to provide retail telephone service, the carrier (at a minimum) would get the same thing as if it had simply purchased the incumbent LEC's finished telephone service and then resold it without the need for interconnection with the incumbent's facilities. There would, however, be one very critical difference—the requesting carrier would obtain the finished telephone service at the cost-based rates provided for in 47 U.S.C. § 251(c)(3), rather than at the wholesale rate separately provided for in the resale provisions of 47 U.S.C. § 251(c)(4).

The Mid-Sized LECs submit that while the Eighth Circuit's decisions on the issues discussed in Part I of this Argument are correct and should be affirmed, the court of appeals unfortunately erred in concluding that the FCC's rules preserved the congressional distinction between resale and unbundled network elements. For several reasons, the decision of the Eighth Circuit on this critical issue should be reversed.[38]

First, the text of several sections of the Act establishes the obligation of incumbent LECs to provide requesting carriers with access to discrete pieces of their network infrastructure. The duty to provide unbundled access to network elements, however, does not require the incumbent to make available all of the network elements necessary to provide a finished retail service, and it certainly does not require the sale of a fully assembled platform of those elements. Thus, section 251(c)(3) provides, in relevant part, that incumbents shall provide "unbundled network elements in a manner that allows requesting carriers to combine such elements to provide . . . telecommunications service." 47 U.S.C. § 251(c)(3).[39] Section 251(d)(2) expressly limits an incumbent LEC's obligation to provide access to proprietary elements of its network. 47 U.S.C. § 251(d)(2).

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[38] In supporting their cross-petition on the merits, the Mid-Sized LECs do not wish to repeat all of the arguments made by the BOCs and GTE in support of their cross-petitions. The Mid-Sized LECs therefore respectfully refer the Court to the briefs filed this day by the BOCs and GTE and incorporate the arguments in those briefs by reference.

[39] Notwithstanding the plain language of section 251(c)(3), the FCC's unbundled access rules require the incumbent, not the requesting carrier, to bear the burden and expense of combining unbundled network elements. *See* 47 C.F.R. § 51.315(c)-(f) (Pet. App. 294a); *see also* FRO ¶¶ 294-95 (J.A. 552-53). The Eighth Circuit properly vacated these rules as contrary to the plain language of section 251(c)(3) (Pet. App. 52a-53a, 70a-71a), and the FCC does not challenge that ruling.

Second, the interconnection and unbundled access sections of the Act are integrated, interdependent provisions. Congress plainly intended that a requesting carrier would obtain access to the unbundled elements of an incumbent's network through physical interconnection with the incumbent's network. Thus, the right of interconnection necessarily implies that the requesting carrier has some facilities of its own to interconnect with the incumbent's facilities. Under the FCC's rules, however, a requesting carrier without any of its own network facilities can purchase a fully operational platform of network elements from the incumbent. Indeed, since the FCC has deemed operator and directory assistance services to be network elements, the requesting carrier can even require the incumbent to perform those services on its behalf. The net effect of the Eighth Circuit's acceptance of the FCC's rules is to permit a carrier that has no facilities of its own to obtain finished telephone service at cost-based prices. This necessarily obliterates the distinction between resale and unbundled elements that Congress was careful to create, and without which true competition from facilities-based competitors will never occur.

Third, the FCC's interpretation of the Act can lead only to what Congress itself feared: the inability of small and mid-sized LECs to withstand the economic calamity of new entrants picking off their large business customers by offering telephone service entirely with recombined unbundled elements priced at cost, rather than at an avoided-cost discount from the higher retail rate that state commissions have required LECs to charge business customers to support residential service. The House specifically amended its bill going into Conference to ensure that LECs need only provide resale at "wholesale rates" rather than "at economically feasible rates to the reseller." *Compare* 141 Cong. Rec. H8426 (§ 242(a)(3)) (daily ed. Aug. 4, 1995) *with id.* at H8444, col. 2 ("resale" amendment). Representative Dingell explained that the amendment was necessary to eliminate the requirement

that "local telephone companies . . . subsidize the long distance competitors," by "requir[ing] service which cost $25 to be sold to AT&T for $6; something which would have caused the necessity of subsidizing, then, AT&T at the expense of small business and local [residential] phone user, an outrageous situation." *Id.* at H8452 (also noting that Reps. Bliley and Fields worked to correct "this failure" in the bill).

It is readily apparent from a reading of the First Report and Order that the FCC anticipated that its rules obliging incumbents to provide new entrants with access to the full array of network elements necessary to provide retail telephone service would be attacked for eviscerating the resale provisions of the Act. Accordingly, the FCC sought to justify its rules by arguing that requesting carriers seeking to provide telephone service solely through the purchase of network elements, rather than through resale, assumed economic risks that were not present in the resale context. As a result of these purported risks, the FCC asserted, its rules did not obliterate the Act's resale provisions. Specifically, the FCC stated:

> A carrier purchasing unbundled elements must pay for the cost of that facility, pursuant to the terms and conditions agreed to in negotiations or ordered by states in arbitrations. It thus faces the risk that end-user customers will not demand a sufficient number of services using that facility for the carrier to recoup its cost. . . . A carrier that resells an incumbent LEC's services does not face the same risk.

FRO ¶ 334 (J.A. 573-74).

However, the FCC's economic argument is based on assumptions, not facts. Furthermore, actual experience proves those assumptions to be false. For example, as GTE and several BOCs pointed out to the court of appeals,[40] a number of state commissions have taken the

[40] *See* Brief of GTE, SBC Communications, Inc., BellSouth Corporation and US West on Petition for Rehearing at 12 n.3, *Iowa Utilities Bd. v. FCC*, No. 96-3321 (8th Cir., filed Aug. 19, 1997).

position that requesting carriers can purchase or lease network elements on an "on demand" basis. Thus, a requesting carrier that has purchased a network element is only required to pay the incumbent for those times when the network element is actually in use by a customer. Such an arrangement thoroughly undermines the FCC's differential economic risk analysis, which was critical to its argument that its rules do not transform the resale provisions of the Act into mere vestiges.

For the foregoing reasons, the Mid-Sized LECs ask the Court to reject the FCC's position that incumbents must provide requesting carriers with access to *all* of the network elements necessary to provide retail telephone service and to vacate that part of the Eighth Circuit's decision upholding that position. However, if the Court should decide that the Eighth Circuit did not err in affirming the FCC's position, then at a bare minimum the Court must reject the FCC's effort to revive 47 C.F.R. § 51.315(b), which provides, "Except upon request, an incumbent LEC shall not separate requested network elements that the incumbent LEC currently combines." Pet. App. 294a. The Eighth Circuit (*see* Pet. App. 71a) vacated Rule 315(b) as inconsistent with section 251(c)(3) which, by its terms, only obligates incumbent LECs to provide access to network elements on an unbundled, *i.e.*, physically separated, basis.

The FCC and AT&T argue that Rule 315(b) simply prevents an incumbent from imposing gratuitous costs upon a requesting carrier by disassembling network elements that it currently combines, forcing the requesting carrier to bear the expense of reassembling them. FCC Br. 17; AT&T Br. 35-36. Thus, since incumbents already "currently combine" all of the network elements they use to provide finished retail telephone service, they should not be required to disconnect those network elements when the full array is purchased by a requesting carrier. This proffered justification for Rule 315(b) is, however, noth-

ing more than a post-hoc explanation of the Rule invented to create a loophole in the Eighth Circuit's initial decision prior to rehearing.

The FCC's current interpretation of and rationale for Rule 315(b) is quite different from the FCC's view in its First Report and Order. There, the FCC stated that under its interpretation of 47 U.S.C. § 251(c)(3), an incumbent is required to provide "as a single, combined element, facilities that could comprise more than one element. This means, for example, that, if a state commission requires incumbent LECs to provision subloop elements, incumbent LECs must still provision a local loop as a single, combined element when so requested, because we identify local loops as a single element in this proceeding." FRO ¶ 295 (J.A. 553). Thus, through Rule 315(b), the FCC simply sought to prohibit incumbents from unbundling certain network elements that could alternatively be viewed as a combination of several subelements. Nothing in the First Report and Order supports a reading of the rule as requiring an incumbent to turn over a fully assembled platform of network elements at cost-based rates.

However, after the Eighth Circuit invalidated the FCC's rules imposing the obligation to combine network elements on the incumbents (*see* page 55 n.39, *supra*), AT&T suddenly imbued Rule 315(b), which the court of appeals had not initially vacated, with an entirely new meaning. Specifically, AT&T argued in state commission proceedings that because an incumbent LEC "currently combines" all of the elements necessary for providing retail service to its own customers, Rule 315(b) prohibits the LEC from providing elements as separate, unbundled elements and requires the LEC instead to provide those elements "in combined form" at no extra charge.[41]

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[41] *See* Brief of GTE, SBC Communications, Inc., BellSouth Corporation and US West on Petition for Rehearing at 6 n.1, *Iowa Utiliites Bd. v. FCC*, No. 96-3321 (8th Cir., filed Aug. 19, 1997).

By challenging the Eighth Circuit's invalidation of Rule 315(b), the FCC seeks to reopen a claimed loophole in the court's original decision that the Eighth Circuit properly closed in its decision on rehearing. To the extent that the FCC, AT&T and others viewed Rule 315(b) as requiring an incumbent to provide requesting carriers with a pre-combined platform containing *all* of the network elements necessary to provide finished telephone service, the Eighth Circuit properly rejected that rule as contrary to the "careful distinctions Congress has drawn in [47 U.S.C.] subsections 251(c)(3) and (4)." Pet. App. 71a.

III. THE FCC UNREASONABLY EXPANDED THE DEFINITION OF "NETWORK ELEMENTS."

Just as its rules on access to network elements eviscerated the resale provisions of the Act, the FCC's interpretation of the term "network element" is so unreasonably broad as to render meaningless the distinction between network elements and telephone services themselves. The Eighth Circuit erred in deferring to the FCC's unreasonable construction of this critical term of the Act.

The Act defines a network element as a "*facility or equipment used in the provision* of a telecommunications service," including the "features, functions, and capabilities that are provided *by means of such facility or equipment*, including subscriber numbers, databases, signaling systems, and information sufficient for billing and collection or used in the transmission, routing, or other provision of a telecommunications service." 47 U.S.C. § 153(29) (emphasis added). The crucial distinction that Congress drew between telecommunications "facilities or equipment" and the use of such to provide a telecommunications "service" shows that Congress rooted the definition of "network elements" in the *physical* parts or equipment of a network —loops, switches, etc.—including the "features, functions, and capabilities" provided by those physical elements.

Nevertheless, the FCC's network element rules distort beyond recognition the equipment/service distinction that is at the core of the network element definition. Thus,

significantly, the FCC's rules require incumbent LECs to provide unbundled access to their Operations Support Systems functions ("OSS"). *See* 47 C.F.R. § 51.319(f) (Pet. App. 301a). Those software systems, frequently proprietary in nature, include pre-ordering, ordering, provisioning, maintenance and repair, and billing functions supported by an incumbent's databases. Obviously, these software, databases and support systems are not physical elements of a network. They play no role in the physical delivery (*i.e.*, transmission or routing) of a telephone call. Rather, as their name suggests, they are business *support systems* that an incumbent uses to, among other things, process orders, dispatch repairmen, and keep track of a customer's service requests. Yet, in an invasion into the incumbent's business of extraordinary proportions, the FCC's rules require the incumbent to turn these important management systems over to the incumbent's competitors. The FCC has thus recklessly exposed business management systems that are critical to the operation of the LEC's own business to interface and other demands from the LEC's competitors that may conflict or compromise those systems. Anyone who has attempted the relatively simple task of interconnecting a home computer to an office network should understand the enormity of, and potential risks associated with, what the FCC has done. Congress could not have intended the LEC's competitors to have such unmitigated power over the systems that allow the LEC to control its own business.

The FCC's rules also improperly require incumbent LECs to provide unbundled access to their directory assistance and operator services. *See* 47 C.F.R. § 51.319(g) (Pet. App. 301a). Plainly, human operators are not "facilities or equipment," nor are they "features, functions or capabilities" provided by means of such "facilities or equipment." Requiring incumbents to make these personnel available to competitors obviously has nothing whatsoever to do with unbundling the pieces of the "network" that are actually used to deliver telephone calls. To hold

otherwise would expand the scope of "network elements" to include virtually all of the live support staff that a LEC employs to run its business operation. The absurdity of defining the term so broadly is reflected in an FCC determination that when a requesting carrier, such as AT&T, purchases unbundled access to a LEC operator, the operator must identify himself or herself as an AT&T operator whenever serving an AT&T local service customer. FRO ¶ 537 (J.A. 680). Given this determination, it is no stretch to imagine the FCC next requiring LEC telephone repair personnel to carry different velcro-backed uniform labels with the names of all requesting carriers and to attach the appropriate label to their uniforms whenever providing home repair services to a customer who subscribes to a particular requesting carrier.

Nevertheless, the Eighth Circuit upheld the FCC's characterization of operator services and directory assistance as "network elements" based on a construction of that term that, upon even a cursory inspection, proves to be as unbounded as the FCC's construction. The Eighth Circuit reasoned that because a "telecommunications service" is the "offering of telecommunications for a fee directly to the public" (47 U.S.C. § 153(46)), then any time a facility assists an incumbent in managing the business aspects of its operation, and thus incidentally assists the incumbent in providing retail telephone service, the facility is somehow "used in providing a telecommunications service." Pet. App. 42a-43a. As with the FCC's definition, however, if the court's construction were correct, anything and everything that assists an incumbent in the business aspects of its operation could be deemed a network element. Under the FCC's unbundling rules, all such elements would then have to be made available to a requesting carrier at cost-based rates. For example, office and repair personnel would be network elements, as would office equipment such as desks and personal computers. Once again, Congress could not have intended such an absurd result.

Finally, the Eighth Circuit erred in accepting the FCC's definition of network elements to include a LEC's "vertical services," such as caller ID and call waiting. Pet. App. 41a, 44a-45a. There is no dispute that these services are retail services that LECs must make available to requesting carriers but at wholesale rates. Yet, it is the FCC's position that these services are also discrete network elements that a requesting carrier can purchase from a LEC on an unbundled basis at cost-based rates. Treating vertical services as network elements eviscerates the Act's distinction between resale and unbundled elements and flies directly in the face of legislative history establishing that Congress decided that "services" were *not* to be included in the definition of network elements. *See* H.R. 1555 § 242(a)(2), 104th Cong., 1st Sess. (May 3, 1995) (unbundling provision of House bill originally applied to "services, elements, features, functions, and capabilities," but Conference Committee later eliminated term "services").

The FCC cannot justify the inclusion of caller ID and call forwarding within the scope of a LEC's unbundling obligations by reference to language in the Act's definition of network elements stating that such elements include "*information* . . . used in the transmission, routing, or *other provision* of a telecommunications service." 47 U.S.C. § 153(29) (emphasis added). According to the FCC, the phrase "other provision" expands the category of network elements to include *any* information related to the provision of telecommunications service. FRO ¶ 261 (J.A. 537-38). Such a construction of the Act, however, ignores settled principles of statutory interpretation that require a word to be interpreted in context. In particular, it ignores the principle of *ejusdem generis*, which requires general terms in a statute to be interpreted in accord with more specific terms preceding it. *See, e.g., Federal Maritime Comm'n v. Seatrain Lines*, 411 U.S. 726, 733 (1973). This principle requires the reference to "other provision" to be interpreted in accord with the specific

terms—"transmission" and "routing"—that precede it. The reference to "other provision" thus simply acknowledges that there are a series of discrete functions known by different technical names involved in transmitting a telephone call from one point in a network to another. In addition to "transmission" and "routing" there are signaling, switching, terminating, etc. Rather than reciting an exhaustive list of these terms, the Act uses a shorthand to encompass them all. Vertical services like call waiting and caller ID, however, are not involved in transmitting a call from point to point. Therefore, they are not "network elements," and the Eighth Circuit erred in upholding the FCC's inclusion of those services within the incumbent LEC's obligation to provide access to unbundled network elements.

CONCLUSION

For the foregoing reasons, this Court should affirm the judgment of the court of appeals in *Iowa Utilities Board v. FCC*, except that the Court should reverse the judgment insofar as it upheld the following: (1) the FCC's ruling that entrants—without using any of their own facilities—may rely solely on the purchase of network elements, at cost-based prices, to provide local service; and (2) the FCC's expansion of the statutory definition of network elements to include OSS, directory assistance, operator services, and vertical services.

Respectfully submitted,

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